ALVIS PLC

ANNUAL REPORT

2003

Financial Highlights

	2003	2002
	£m	£m
Orders received	**420.6**	149.7
Turnover	**348.8**	225.7
Group profit before exceptional items, goodwill and tax	**19.8**	16.5
Group profit before tax	**20.3**	14.5
Group profit after tax	**20.4**	10.1
	p	p
Basic earnings per ordinary share before exceptional items and goodwill	**18.6**	10.4
Basic earnings per ordinary share	**19.3**	9.1
Dividends per ordinary share		
Interim paid	**2.5**	2.3
Final proposed	**–**	3.7
	2.5	6.0

Financial Calendar

Annual General Meeting	29 April 2004
Interim results	15 September 2004
Financial year end	31 December 2004

Contents

SEP

The Alvis Group of Companies

Alvis plc is one of the world's leading companies in armoured vehicles and other specialist military vehicles. Its business is conducted through its various operating subsidiaries: Alvis Vickers Limited in the UK, (including Alvis Bridging), Alvis Hägglunds AB in Sweden and Alvis South Africa (Pty) Limited.

The Alvis Group has the largest product range of any equivalent company, successful international partnerships with other major companies, and vehicle products in service with the armed forces of more than fifty countries worldwide. Having successfully expanded on its experience in armoured vehicle engineering, Alvis is now a specialist in the integration of high technology defence systems and digital technology.

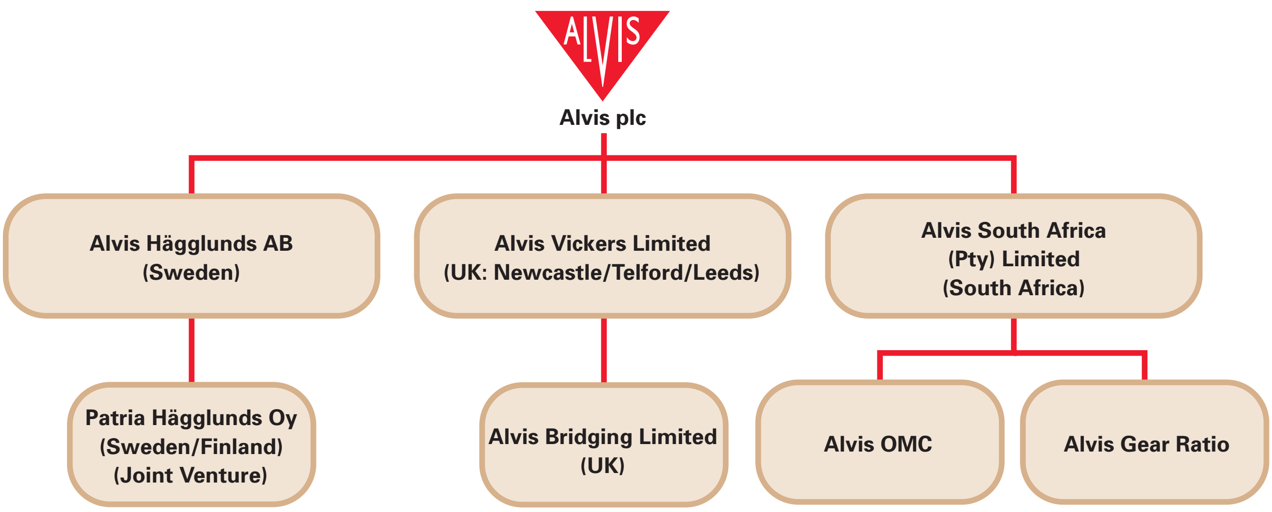
The strategic aim of Alvis is to achieve profitable growth in the world market for armoured vehicles and related defence products and services, fulfilling in the process the highest aspirations of our customers, employees and shareholders.

Alvis Vickers Limited was formed in 2002, following the merger of Alvis Vehicles Limited and Vickers Defence Systems. In addition to its headquarters and main manufacturing plant in Newcastle-upon-Tyne, Alvis Vickers has a modern engineering/product support facility in Telford and an engineering/technology centre in Leeds. Alvis Bridging, is based in Wolverhampton and produces modular bridging systems. Alvis Vickers employs approximately 1000 personnel throughout its UK sites. In addition to exporting vehicles internationally, Alvis Vickers has supplied over 90% of the British Army's armoured vehicle fleet. Alvis Vickers' products include Challenger 2, Trojan/Titan Engineer Tanks, Scorpion, Scimitar, Stormer, Warrior, Piranha, Tactica, Scarab, Supacat and Multi-role Light Vehicle (MLV), as well as the BR90 and ATLSB bridging systems.

Alvis Hägglunds AB was acquired by Alvis plc in 1997. Alvis Hägglunds is based in Örnsköldsvik, Sweden, where it employs approximately 1000 personnel in a large, purpose-built facility.

Employing the Group philosophy of innovative design solutions, continuous product development and high quality production methods, Alvis Hägglunds' products are the market leaders in their field and include the CV90 Infantry Fighting Vehicle family, the Bv range of all terrain vehicles, AMOS mortar system (with joint venture partner, Patria of Finland) and SEP, a new tracked or wheeled armoured vehicle.

Alvis plc owns a 75% interest in **Alvis South Africa (Pty) Limited** which was acquired by Alvis in 2002 as part of the Vickers Defence acquisition. Alvis South Africa employs approximately 540 personnel and trades through its two divisions: Alvis OMC and Alvis Gear Ratio. Alvis OMC is South Africa's primary military vehicles facility, based in Benoni, near Johannesburg. Specialising in mine protection, Alvis OMC produces heavy and light armoured vehicles, in tracked and wheeled configurations, Alvis OMC products include the RG range, Rooikat, Kobra, G6 and Wasp. Alvis Gear Ratio is located in Alrode, near Johannesburg, where it designs and manufactures transmission systems, drive lines and components for the local and overseas market.

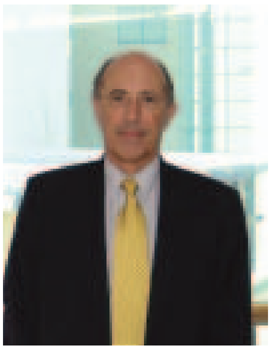


Nicholas Prest CBE MA (Chairman & Chief Executive)

Age 50. He joined the Group in 1982 from the MoD Export Services Organisation and became Head of Export Marketing from 1983 until elected to the Board in 1985 as Marketing Director. He was appointed Deputy Chief Executive in May 1989 and Chief Executive in December 1989 and became Chairman in 1996.

Sir Robert Hayman-Joyce KCB CBE DL *#

Age 63. He joined the Board as a Non-executive Director in September 1999. He retired from the British Army in early 1999 as a Lieutenant-General following a distinguished career in the Royal Armoured Corps and in the Defence Procurement Agency. In his last position, he was Deputy to the Chief of Defence Procurement, Master General of the Ordnance and a member of the Army Board. He is Chairman of Raytheon Systems Limited.



David Wright CBE *#

Age 64. He joined the Board in November 1998 as a Non-executive Director. He was, until his retirement on 31 December 2000, an Executive Director of GKN plc, and is a Director of Raytheon Systems Limited. He is Chairman of the Audit Committee.

Martin Greenslade MA ACA (Finance Director)

Age 39. He joined the Board and was appointed Finance Director in March 2000. He was previously Managing Director of MNB Maizels Ltd, the UK investment banking division of MeritaNordbanken and a corporate finance executive of Enskilda Securities, London. Prior to that he was with Coopers & Lybrand, London.

Trevor Beyer BCom ACA (Senior Independent Director)*#

Age 67. He joined the Board as a Non-executive Director in May 1993. He is Chairman of the Remuneration Committee and the Nominations Committee and has been Chairman of the Audit Committee. He is a Director of Guinness Peat Group Plc, Lion Capital Partners plc, Newbury Racecourse Plc, Dawson International Plc and Nationwide Accident Repair Services Plc.

Company Secretary: P E Jarman MA, Solicitor

*Member of the Audit Committee
Member of the Remuneration Committee
All Directors are Members of the Nominations Committee

Photographs taken at Alvis Vickers' new Centre for Electronic and Systems Technology, Leeds, UK

Combat Vehicles Tracked

Challenger 2
Challenger 2 is the new generation Main Battle Tank (MBT) in service with the British Army and the Royal Army of Oman. Employing advanced fire-control and armour technology, it is the British Army's premier system for ground combat.

Scorpion & Stormer
Proven world-wide and in service in 23 countries, Scorpion is a tracked, air portable reconnaissance vehicle and light tank, weighing less than 10 tonnes and designed for a multi-role capability. Many Scorpion Family vehicles are in service with the British Army where it is known as CVR(T). Stormer is a larger multi-role platform. It is built in the same combat-proven alloy armour as Scorpion and shares its very high level of tactical and strategic deployability.

CV90
The CV90 family is the most modern tracked, armoured vehicle currently in series production in the 20-30 tonne range. CV90 has exceptional mobility, firepower and protection, supported and coordinated by digital information and control systems of Alvis Hägglunds' design. In service with the Swedish and Norwegian armies, it is currently in production for Switzerland and Finland.

Warrior
Warrior is a tracked infantry fighting vehicle family. More than 1000 vehicles are in service with the British and Kuwait armies, and the vehicle is proven in combat and peace keeping roles internationally.

SEP/FRES
FRES and SEP are new land systems programmes in the UK and Sweden. Both call for a new family of armoured platforms combining high levels of protection, mobility, and firepower and battle-winning digital technology with low weight to assure rapid deployability and lower logistic burden. Alvis is developing technologies to meet both programmes.

Combat Vehicles Wheeled

Wasp
Wasp is a highly mobile, rapid deployment reconnaissance vehicle, capable of transporting a 2-3 man crew in front plus five men or equipment in the rear. Designed particularly for airborne forces, four vehicles can be transported in a C-130 Hercules and it can also be carried underslung a helicopter.

Piranha
Internationally proven, Piranha is a wheeled armoured vehicle in the 14-20 tonne range. Piranha is available as personnel carrier, transport, command, ambulance, recovery, mortar and NBC reconnaissance vehicles

Combat Support Equipment

Military Bridging Systems
The Alvis Modular Bridging System, known as BR90 in the British Army, played a key role in the recent operations in Iraq. Seen here is a 34m general support bridge, used by the Royal Engineers to span a demolished section of the Rumaylah bridge. The Alvis Modular Bridging System has been used in the UK, Germany, Kosovo, Macedonia, Bosnia, Canada, Poland and Iraq and has recently been bought by Malaysia.

Trojan
Based on a Challenger 2 chassis, Trojan is a new engineering tank, currently undergoing trials for the UK MoD. It has an excavator arm and can be fitted with an interchangeable mine plough or dozer blade. Trojan is a versatile, multi-purpose vehicle which will be used primarily in the support of military combat operations. Its main task will be to clear complex obstacles under fire. Trojan will enter service with the British Army in 2005.

Titan

Titan is a new bridge-layer vehicle, based on a Challenger 2 chassis, and presently undergoing trials in the UK. Titan can launch a 26m close support bridge (also made by Alvis) under armour within two minutes, making it the fastest in the world. Titan can lay multiple combination bridges. Titan will enter service with the British Army in 2005.

All Terrain Vehicles

Bv206 and Bv206S

11,000 Bv vehicles are in service in 40 countries. Fully amphibious, and designed to cross the most extreme terrain, these versatile vehicles have a wide range of applications in combat support roles. Bv206S is the new, improved, armoured version, recently deployed by KFOR, Kosovo. Bv206S has been bought by Sweden, France, Italy, Germany and Spain.

BvS10

The BvS10 is the latest armoured version of the Bv family. Larger than the Bv206S and with improved load capacity and performance, it retains the same superior mobility. BvS10 has been selected by the British Royal Marines for their new All-Terrain Vehicle (Protected) programme, supplementing their existing fleet of Bv206 vehicles.

Security Vehicles

Tactica

The Tactica family is a complete range of armoured 4x4 vehicles available in a wide range of variants including explosive ordnance disposal. Tactica has been designed for use in police and other security roles and for low intensity military operations.

RG-12

Originally developed as an internal security vehicle, RG-12 is also available as a command vehicle, armoured ambulance, armoured logistics carrier, personnel carrier and surveillance vehicle. Over 700 RG-12s are in service in eight countries world-wide.

Utility Vehicles

Multirole Light Vehicle (MLV)

MLV has been selected for the British Army's Future Command and Liaison Vehicle (FCLV) requirement. The versatile and highly mobile MLV weighs 7 tonnes and can be configured for a wide variety of roles. Modular upgradeable armour panels provide excellent protection for the crew.

RG-31

The RG-31 Nyala is a mine protected, multi-role, light armoured vehicle. It has been successfully deployed with the UN in Bosnia and Lebanon and is also in service with the US Army and several other forces. RG-31 is available as an armoured personnel carrier or utility vehicle and can be adapted to a variety of other applications.

RG-32M

The RG-32M family of utility vehicles fulfils roles requiring high levels of payload and capacity, combined with anti-tank mine protection. RG-32M is the latest development in the RG-32 range, which has been successfully deployed on world-wide operations with international UN missions and other security and combat forces.

Turret Systems

AMOS

AMOS is a turreted, smoothbore, twin barrel 120mm mortar system, incorporating automatic loading, digital maps, navigation and fire control, giving the weapon system autonomous capability. AMOS is under development by Patria Hägglunds, a joint venture between Alvis Hägglunds and Patria Industries of Finland, for the Finnish Army.

Results

In the year ended 31 December 2003 Group sales were £348.8m (2002: £225.7m), profit before tax, goodwill and exceptional items was £19.8m (2002: £16.5m) and profit before tax was £20.3m (2002: £14.5m). Group profit after tax was £20.4m (2002: £10.0m) and earnings per ordinary share were 18.6p before goodwill and exceptional items (2002: 10.4p) and 19.3p after goodwill and exceptional items (2002: 9.1p).

Notable changes to the composition of the 2003 profit before tax, exceptionals and goodwill as compared with 2002 were:

- an increase in trading profit at Alvis Hägglunds from £12.4m in 2002 to £19.6m in 2003,
- a reduction in trading profit in the UK from £4.9m in 2002 to £2.8m in 2003,
- a trading profit at Alvis South Africa of £0.8m (2002: £0.1m),
- an increase in the trading loss at Alvis Moelv from £1.2m in 2002 to £2.3m in 2003.

The improved trading profit at Alvis Hägglunds arose from a substantial increase in sales from £104.1m in 2002 to £175.7m in 2003. The biggest factor in the sales increase was the ramp up of serial deliveries of CV90 to Switzerland. Serial deliveries of CV90 to Finland also commenced in the year.

In the UK sales increased from £107.4m in 2002 to £133.9m in 2003 as a result of the incorporation for a full year of the former Vickers Defence businesses. However, on a pro forma basis sales were lower in 2003 than those posted by the companies as separate entities in 2002, and the cost base of the combined business in relation to revenue available in 2003 caused a reduction in trading profit.

The Group's net funds position at 31 December 2003 was £80.0m (2002: £65.3m). The increase reflected a good performance on milestone payments on major projects and the receipt of £15.7m as a working capital related price adjustment, net of further costs on the acquisition of Vickers Defence.

Operations

Alvis Hägglunds faced the task of building up production on three major new programmes simultaneously in 2003, being ATV(P) for UK, CV90 for Switzerland, and CV90 for Finland. ATV(P) is a completely new product, the CV90 specification for Switzerland is a substantial advance on previous build standards, and the Finnish specification is different again. The challenges in engineering, manufacturing and supplier management have been largely surmounted, and Alvis Hägglunds performed well in boosting their sales by over 65% in a year.

Alvis Vickers had to manage a major reorganisation and a demand from the UK MoD for exceptional support for Operation Telic in Iraq, whilst at the same time maintaining focus and programme performance on major projects, including MRAV and the new Titan/Trojan Engineer Tanks. These goals were largely accomplished. The company performed exceptionally well in meeting the demands of Operation Telic, which included the deployment of over 50 staff to Kuwait to fit urgently required upgrade kits to Challenger 2 tanks. The whole episode showed the importance of the UK industrial base to the fighting ability of the Armed Forces, and the company was publicly thanked by the MoD for its contribution.

Alvis Bridging made a small profit in the year. Effort was mainly concentrated on engineering and manufacturing work for a new bridging system for Malaysia which is due for delivery in 2004.

In South Africa, Alvis OMC made a small operating profit, being limited by slow order intake in the export market, whilst Alvis Gear Ratio performed well.

CV90 FAMILY

Alvis Vickers Reorganisation

As reported at the half-year, the integration of the Vickers Defence businesses into the Alvis Group has gone well. The new Alvis Vickers management team under the leadership of Trevor Harrison has come together effectively. The main changes in 2003 were: a reduction in administrative staff to eliminate duplicated functions; the creation of a business headquarters at Newcastle with associated moves of staff from Telford; the move of Leeds-based staff to a new facility forming the company's centre of excellence for systems engineering and electronics; and the concentration of Telford staff onto the main production site, allowing the leased office block to be vacated.

An exceptional charge of £2.0m was made at Alvis Vickers in 2003, which, together with the charge of £2.0m taken in 2002, covered the cost of these restructuring moves.

In January 2004 a further phase of reorganisation was announced, involving a major reduction of manufacturing activities on the Telford site. A charge of £3.5m will be taken for this in 2004. Overall we do not expect the cash cost of the reorganisation consequent on the acquisition of Vickers Defence and the creation of Alvis Vickers Limited to exceed the £7.5m announced at the time of the acquisition.

A further charge of £1.5m will be taken in 2004 to cover the cost of a reduction in engineering manpower to match resources to the workload now forseen.

Completion of these elements of reorganisation will result in an overall reduction in annual costs of some £9.0m. Moreover, the acquisition of Vickers Defence has significantly enhanced the market position of Alvis, particularly in the UK, and we are confident that it will bring considerable benefits in the future.

Alvis Moelv

Alvis Moelv had made a loss in recent years due to a very narrow market position, programme cancellations and postponements, and a difficult, high cost operating environment. In January 2004 it was announced that Alvis Moelv would close later this year. A charge of £3.5m will be taken in 2004 to cover the cost of closure, the majority of which relates to future rental costs of the facility.

People and Organisation

There were no changes in the composition of the Alvis Board in 2003. Following the departure of GKN from the share register, David Wright, formerly the GKN nominee, has remained on the Board as an independent Non-executive Director. The Board values his experience and input. David has succeeded Trevor Beyer as Chairman of the Audit Committee. Trevor Beyer is chairman of the Remuneration and Nomination Committees. The Board has examined its own composition and procedures carefully in the light of the requirements of the business and prevailing corporate governance guidelines, and believes they are appropriate. We will keep them under review as the business develops.

Orders

The Group's order intake in the year was £420.6m (2002: £149.7m). The order book at 31 December 2003 stood at £892.6m (2002: £781.1m). Of this £404m was at Alvis Vickers, £438m at Alvis Hägglunds, with the balance at Alvis Bridging and Alvis South Africa.

Major orders received in the year included the FCLV programme for the UK at Alvis Vickers (£142m), and Bv206S for Italy and AMOS development for Finland at Alvis Hägglunds (£57m and £31m respectively). Spares and maintenance orders across the Group exceeded £85m, whilst upgrade orders exceeded £50m. This shows the strength of recurring business arising out of the Group's large installed vehicle base.

Prospects

Based on deliverable orders on hand for 2004 and a normal anticipated level of recurring business, we expect the Group to make some further progress in 2004. The outlook for 2005 is better, with growth in sales anticipated at Alvis Vickers as the Titan/Trojan programme moves into series deliveries. Progress would be further enhanced by additional export orders at Alvis Vickers. We continue to pursue some major export campaigns, primarily in the Middle East. We remain optimistic about a positive outcome to these efforts, but timing remains, as ever, difficult to judge. At Alvis Hägglunds we are pursuing good prospects for major additional CV90 and all-terrain vehicle orders, mainly in Europe.

MLV

The future of the UK market is very important for Alvis in the medium and long term. Whilst we were disappointed at the UK's withdrawal from MRAV, the prospect of business growth from the UK market remains, particularly in the Future Rapid Effect System (FRES) programme. FRES, which has superseded elements of MRAV, is a programme for a range of new armoured platforms which will be at the heart of the British Army's future rapid reaction capability for worldwide operations and of the UK MoD's drive to establish Network Enabled Capability.

FRES is expected to start with an assessment phase in 2004, and the Alvis Group is well placed to contribute to this and the subsequent demonstration and manufacturing phases. The acquisition of Vickers Defence has brought additional skills in systems engineering, software and electronics, which are vital to programmes such as FRES.

In Sweden there is interest in developing a new light armoured vehicle (SEP programme). Alvis Hägglunds has already completed extensive study and technology demonstration work for SEP. There are potential overlaps between SEP and FRES, and Alvis Vickers and Alvis Hägglunds are working closely together to maximise their contribution to both programmes and the potential benefits of linkage between them.

Recommended Offer

As separately announced, the Board is recommending a cash offer for the Company of 280p per share from General Dynamics for the reasons stated in the offer announcement.

Dividend

In view of the offer, the Board is not recommending a final dividend for 2003. Should the offer be unsuccessful and Alvis remain an independent company, the Board intends to declare an interim dividend of 4.0p per share in lieu of the 2003 final dividend.

Nick Prest
Chairman and Chief Executive

	2003 £m	2002 £m
Sales	**133.9**	107.4
Profit before interest, tax, exceptional items and goodwill	**2.8**	4.9
Orders received	**238.1**	93.1
Order backlog at year end	**428.2**	326.0
Private venture research and development	**2.2**	3.6

Performance Overview

Sales in 2003 increased relative to 2002 due to the addition of turnover from the former Vickers Defence businesses. However, turnover at the former Alvis Vehicles business in Telford was lower than in 2002 and, pending reductions being achieved through restructuring, the higher cost base in 2003 in proportion to the revenue available led to a lower operating profit.

Major Programmes and Deliveries

The largest programme running at Alvis Vickers is the Engineer Tank System (ETS). Effort in 2003 was concentrated on development and prototyping work. Two Trojan and two Titan prototypes are now on reliability trials and the programme is meeting its objectives.

Following the UK MoD's announcement that it would be withdrawing from the MRAV programme on account of a change in perception of future requirements for deployability, work stopped on the UK-specific aspects of the programme. Work continues for the common programme, including four prototypes to be delivered in the first half of 2004. Discussions continue about the future industrial arrangements for the remaining Dutch/German programme, but it is not expected that Alvis will have a long-term involvement. Deliveries of new Tactica AT 2000 vehicles to the Norwegian Air Force commenced in 2003. This is the first production run of the updated Tactica vehicle.

Alvis Vickers is playing a substantial role on the Bowman radio programme in the design and certification of the radio installations on Alvis vehicles. This was a major activity in 2003.

Technology and Product Development

Alvis Vickers has established an integrated strategy for the development of key technologies and capabilities and linked to this a centre of excellence for systems and electronics has been created at Leeds.

Company funded technology and product development has included lightweight ceramic armour, and health and usage monitoring systems.

Alvis Vickers has also continued to work on a number of new technology insertion programmes for Challenger 2 for which the company has now received contracts. These include a system known as P-BISA, which, coupled to the new Bowman communications system, will be at the heart of the British Army's concept of network enablement.

Work on FRES concepts and technologies has continued during the year. In particular, Alvis Vickers and Alvis Hägglunds have made significant progress on tracked vehicle E-drive development, which has the potential to be a key enabling technology for FRES.

Orders Received and Business Development

In the export market Alvis Vickers has continued to pursue a number of major order opportunities, principally in the Middle and Far East.

In November 2003 the UK MoD placed a contract valued at £142m with Alvis Vickers for the MLV vehicle for the FCLV programme. In addition to the 401 ordered, the MoD has options for a further 400 vehicles. MLV also has good export potential.

Contracts for upgrades to the British Army in-service FV430 vehicle have been received during 2003, and progress has been made towards a significant programme to provide new engines and gearboxes.

Alvis Vickers has continued to work with the UK MoD in formulating plans for future armoured vehicle programmes, and in particular FRES. The assessment phase for FRES is expected to commence in 2004, and Alvis Vickers is working to play a significant role.

TROJAN

Operations and Personnel

Alvis Vickers' focus on continually improving its operational effectiveness led to the company winning a national manufacture award in the 2003 IMechE Manufacturing Excellence Awards. The range of systems integration expertise and manufacturing skills now available across the business provides an excellent foundation for all new vehicle requirements.

The company has also received quality accreditation to ISO 9000:2000, 14000 and 18000.

Alvis Vickers has continued to operate a range of staff development schemes, including a substantial graduate engineer recruitment programme.

Product Support

Alvis Vickers has continued to work closely with the MoD to develop further innovative support strategies for vehicles already in service. These are intended to reduce the cost of support to the MoD whilst securing for Alvis Vickers long-term support business. The Base Inspection and Repair contract for Challenger 2 is now well established and vehicles were completed to schedule for 2003.

Alvis Vickers' Product Support and Operations teams were mobilised during 2003 to meet the requirements of Operation Telic in support of the British Army activity in Iraq. The Alvis Vickers team designed, developed and helped install a number of upgrades to Challenger 2 and CVR(T) vehicles. These proved their worth during the conflict ensuring the performance and resilience of these vehicles under operational conditions.

The Product Support organisation continues to support the many Alvis Vickers fleets around the world with service, support and upgrade programmes, the latest being the dieselisation of the Scorpion fleet in Brunei which began in 2003.

Alvis Bridging

The development phase of the UK MoD Pontoon contract was completed during the early part of 2003 with production starting in the middle of the year.

The contract to supply the Malaysian Army with three 52 metre Axially Tensioned Long Span Bridge Systems continues to progress well for delivery at the end 2004.

A new five-year contract has been signed with the UK MoD, commencing 2004 for Contract Logistics Support for the British Army's in-service bridging equipment and includes the storage and maintenance of BR90.

A number of bridging opportunities in the Far East and Europe continue to be pursued.

	2003 £m	2002 £m
Sales	**184.2**	111.7
Profit before interest, tax and exceptional items	**19.6**	11.2
Orders received	**153.2**	49.3
Order backlog at year end	**438.1**	435.6
Private venture research and development	**3.6**	1.7

Performance Overview

In 2003 the Alvis Hägglunds Group increased sales by more than 65% compared with 2002, giving an increase of more than 130% since 2001. Trading profit also increased substantially over 2002 and capacity in both manufacturing and engineering was heavily utilised in support of the large projects commencing production in 2002. Engineering resources were also focused on the new AMOS series order and further studies and work on the SEP project.

Major Programmes and Deliveries

The deliveries of the Finnish and Swiss CV9030 programmes continued and these two projects will be a major part of Alvis Hägglunds' turnover until 2005.

Delivery of the upgraded CV9040C to Sweden was successfully completed. This programme began in 2002 and consisted of 58 vehicles. CV9040C, upgraded with add-on armour, mine protection and air conditioning, will be used by the Swedish international rapid reaction force, which will form part of the EU rapid reaction forces.

Also, 15 Bv206S all-terrain vehicles were delivered to Sweden for use by the rapid reaction force. These vehicles are equipped with automatic climate control, add-on armour and extended mine protection.

Deliveries of an ambulance version of Bv206S to the German Army's rapid reaction force for international service have commenced. This programme is being performed in collaboration with Rheinmetall Land Systems.

The first BvS10 "Viking" for the UK's Royal Marines was handed over to Lord Bach, the UK's Minister for Defence Procurement, on 1 July 2003. It was the first delivery in an order for 108 armoured, all-terrain vehicles, consisting of troop carrying, command and repair and recovery variants. The Vikings will be used by the Royal Marines in worldwide operations.

Bv206S
photo: Paulo Valpolini

Technology and Product Development

Pre-development work for Sweden's SEP programme continued in 2003. SEP is a new modular armoured vehicle concept intended to combine considerably lower vehicle weight (compared with traditional armoured vehicle designs) with extremely high operational flexibility. It is also intended to have substantial development potential, including both tracked and wheeled versions. Key technologies include electric drive, defensive aid suites, vetronic architectures and rubber tracks. The company has already built and tested a tracked demonstrator on behalf of the Swedish Defence Material Administration (FMV) and has now delivered a wheeled demonstrator. In 2003, Alvis Hägglunds was awarded contracts for further engineering studies as well as the manufacture and delivery of hardware items such as test rig systems and a new generation tracked SEP prototype. The work being undertaken includes systems engineering, survivability, man-machine interface, drive system and role studies. A decision regarding full development of SEP will be taken by the Swedish MoD in the next two years.

Work was carried out on the production of a technology demonstrator for the VETEC project and its integration into the SEP tracked demonstrator. VETEC is a joint Swedish-German project aimed at evaluating and developing future electronic architectures for use in military vehicles.

Orders Received and Business Development

In March 2003, Finland placed an order for 24 AMOS Mortar systems with Patria Hägglunds, a joint venture owned by Patria of Finland and Alvis Hägglunds. Deliveries will take place between 2006 and 2009. The contract gives a solid basis for the serial production of AMOS. This order further strengthens the position of AMOS as a leading mortar system. AMOS represents the latest technology in turret systems and is designed to be integrated into a wide range of tracked and wheeled platforms as well as fast combat boats.

During the year Italy has ordered a total of 148 new Bv206S vehicles and upgrades for 52 Bv206 vehicles. This makes Italy the largest customer for Bv206S. The vehicles will be used by the Italian Army's rapid reaction forces, mainly for international missions. This important order further demonstrates the leading position of Alvis Hägglunds in the all-terrain vehicle sector. There are a number of other substantial armoured all-terrain vehicle programmes planned in Europe and elsewhere and Alvis Hägglunds anticipates significant growth in this area of its business.

Operations and Personnel

An extensive programme for increasing the operational efficiency of the workshops, including investment in robotic welding equipment, was completed in 2003. Robotic welding has significantly boosted productivity in the fabrication area and helped Alvis Hägglunds to achieve a large increase in vehicle output with a relatively small increase in production staff.

Alvis Hägglunds has continued to develop the capability of its staff through internal training and selective recruitment of technical specialists. The company now employs more than 230 engineers qualified at degree level. The ability to handle complex design and integration of hardware and software into overall systems solutions has been enhanced by growing expertise and the successful handling of systems integration challenges in major new programmes.

Product Support

It was a successful year for the after sales business, including spares, integrated logistic support and vehicle rebuilding, with sales of £24m.

Consideration is being given within the Swedish Ministry of Defence and FMV to transferring greater responsibility for the maintenance and technical support of armoured fighting vehicles to the Swedish defence industry. Through a co-operation agreement with SAAB, Alvis Hägglunds is in a strong position to offer such services to the Swedish Defence Forces. As a first step in this process, a contract for the supply of all-terrain vehicle spares was awarded on the basis that Alvis Hägglunds will manage the inventory on behalf of the customer.

Other significant contracts secured during the year included the upgrade of CV9030 for Norway for international missions and the provision of training programmes for Switzerland.

Alvis Moelv

A redundancy programme was carried out during 2003. This reflected low order intake and the difficult market of recent years. As discussed in the Chairman's statement, a decision was taken in January 2004 to close the business later in the year.

	2003 £m	2002 £m
Sales	**30.8**	6.6
Profit before interest, tax, exceptional items and goodwill	**0.8**	0.1
Orders received	**35.0**	7.3
Order backlog at year end	**26.3**	19.5
Private venture research and development	**0.3**	0.2

Performance Overview

The 2003 figures reflect a full year trading compared to the three months in 2002 following the acquisition of Vickers OMC on 1 October 2002. Alvis South Africa has two operating divisions; Alvis OMC responsible for vehicle design, assembly and support and Alvis Gear Ratio, a manufacturer of specialised transmissions and components.

The value of the local currency had the largest impact on the year's results. The rand strengthened by as much as 27% against major currencies thereby reducing profits on exports. The overall impact was however limited as 81% of revenue is generated locally.

Major Programmes and Deliveries

The Olifant Upgrade Industrialisation programme was completed during the year paving the way for the production contract.
All major deliverables on the Rooikat and Mamba Upgrade programmes for 76 and 100 vehicles respectively, were completed in 2003.

Technology and Product development

Over the past three years Alvis OMC developed the capability to predict scientifically the effects of a mine blast on a vehicle and its occupants. This work continued in 2003 and enabled Alvis OMC to improve the RG-31's mine protection capability. A flat bottom mine protected test hull was successfully demonstrated to an international audience during a landmine symposium. Significant improvements have been made to the current product range and a new RG-31 mine protected 4-stretcher ambulance was developed and two production vehicles delivered to an international customer.

Orders Received and Business Development

In July 2003 a £2.7 million order was received for the supply of Alvis Wasp vehicles for the "Rapid Deployment Reconnaissance Vehicle" requirement of the South African National Defence Force (SANDF) and in September 2003 a £10.3 million order was received to upgrade Olifant 1B MBT's for the SANDF.

The RG-12 has successfully completed trials in Europe. Potential customers in Europe, South America and the Middle East are currently evaluating the RG-32M.

The Hoefyster requirement of the SANDF for a New Generation Infantry Combat Vehicle is the largest vehicle programme in the immediate future for the SANDF and Alvis South Africa is well placed to play a significant role in this programme. The tendering and demonstration process commences in 2004, and contract awards are expected in late 2005 or 2006.

Operations

Both Alvis OMC and Alvis Gear Ratio achieved ISO 9001:2000 certification in 2003.

Product Support

The product support business achieved sales of £9 million. This business is responsible for the support of most of the SANDF armoured vehicles and includes the management of 32 dealers throughout South Africa.

Alvis Gear Ratio

Sales of £9.6 million were achieved in 2003, a 14% improvement on the same period for the prior year. Alvis Gear Ratio secured a contract from Renk for the supply of gearboxes for European defence projects in 2002. Deliveries of these gearboxes together with the Mamba and Rooikat Upgrade programmes contributed to the growth of this business in 2003.

Building on the successful relationship already established with Bell for supply of transmissions for dump trucks, development of other specialist commercial applications of gearbox technology continued in 2003. Prototypes of new products are currently being tested in South Africa and Australia, and new opportunities in this field are being pursued in the USA.

In recent years Gear Ratio has transformed itself from a business largely dependent on the domestic defence market to one serving a range of military and commercial markets, with the latter in the majority. A plant renewal programme to maintain and boost competitiveness has been an important element of this success, and is continuing.

RG-32M

	1999	2000	2001	2002	**2003**
	53 weeks	52 weeks	52 weeks	52 weeks	**52 weeks**
	£000	£000	£000	£000	**£000**
Results					
Turnover	233,803	203,494	149,415	225,714	**348,843**
Profit before taxation	34,599	12,841	28,172	14,543	**20,263**
Balance sheets					
Fixed assets and investments	56,173	45,145	35,528	49,626	**49,740**
Net current assets	55,140	66,467	138,587	54,463	**78,185**
Creditors due after one year and provisions	(61,488)	(61,407)	(115,675)	(70,778)	**(74,677)**
Minority interests	–	–	–	(3)	**(49)**
Net assets employed	49,825	50,205	58,440	33,308	**53,199**
Share capital	63,985	64,125	58,602	27,265	**27,570**
Other reserves	(11,072)	(9,903)	5,244	11,576	**30,417**
Own shares held in trust	(3,088)	(4,017)	(5,406)	(5,533)	**(4,788)**
Shareholders' funds	49,825	50,205	58,440	33,308	**53,199**
Statistics					
Per ordinary share					
Basic earnings - before exceptional items and goodwill	8.9p	7.3p	6.3p	10.4p	**18.6p**
Basic earnings - after exceptional items and goodwill	26.4p	6.9p	18.2p	9.1p	**19.3p**
Dividends	4.5p	5.0p	5.5p	6.0p	**2.5p**

The Group has adopted Urgent Issues Task Force Abstract 38, Accounting for ESOP Trusts, during the year ended 31 December 2003. As a result, 2002 and prior periods have been restated accordingly.

Operation Telic, Iraq 2003

The page opposite depicts Alvis Group equipment in service with the British Army and Royal Marines during Operation Telic, Iraq, 2003: Challenger 2, Warrior, Scimitar, Bv206 and BR90 modular bridging system.

Quotations from MoD Iraq First Reflections Report and RUSI Conference on the Performance of British Equipment in the War in Iraq:

"Challenger 2 and Warrior: first class fighting equipment…Challenger 2 was exceptionally successful and invaluable… Warrior was able to withstand everything that was sent at it… Industry responded magnificently… The low levels of UK casualties is a reflection of the outstanding protection afforded by our armoured vehicles"

Operating results

The Group's results and the operating performance of Alvis Vickers, Alvis Hägglunds and Alvis South Africa are discussed under the Chairman's Statement and Operations Review.

Acquisition of Vickers Defence

The consolidated results include the performance of the former Vickers Defence businesses for the whole of 2003 (2002: 3 months).

Consideration for the purchase of Vickers Defence was £16.0m, subject to certain working capital adjustments. The final agreement resulted in a payment to Alvis of £16.1m, largely due to contracts on which further work was required at 30 September 2002 but on which no further revenue was due from the customer. In accordance with FRS 7, we have reassessed the fair value of assets and liabilities acquired in the original transaction on the basis of our experience in 2003. This exercise has led to a net reduction in the fair value of liabilities acquired which in turn has altered the goodwill associated with the transaction.

The revised calculation of goodwill results in a negative figure of £2.0m, meaning that we paid £2.0m less in cash than the fair value of the net assets we received. It is worth noting, however, that the goodwill calculation takes no account of the exceptional reorganisation costs which have resulted from the integration of the acquired businesses. £1.4m of the negative goodwill has been credited to the profit and loss account in 2003 and the majority of the balance is expected to be taken in 2004.

Exceptional items

In 2003, an operating exceptional charge of £2.0m (2002: £2.0m) has been taken in respect of the reorganisation of Alvis Vickers following the acquisition of Vickers Defence. As in 2002, the main element of the charge relates to redundancy costs arising from the elimination of duplicated functions. Separately in 2003, we have released, as a non-operating exceptional item, a provision of £1.1m in respect of deferred income on the sale of Barracuda, a former subsidiary of Alvis Hägglunds. Barracuda was sold in 1999 but an element of consideration was contingent on the performance of the business up to 31 December 2004. During 2003, Barracuda achieved the performance targets necessary to secure the release of the deferred income provision and, depending on Barracuda's performance in 2004, additional consideration of up to SEK 5 million (£0.4m) may become payable to Alvis.

Following the announcement in January 2004 of a major reduction in manufacturing activity in Telford, we anticipate an operating exceptional charge of £3.5m in 2004, bringing the total cash cost of reorganisation following the Vickers Defence acquisition to £7.5m. This is in line with our expectation at the time of the transaction. A further operating exceptional charge of £1.5m will be taken in 2004 to cover the cost of reduction in engineering manpower to match resources to the workload now foreseen. In Norway, our announcement in January 2004 that Alvis Moelv would close later in the year will result in a non-operating exceptional charge in 2004 of £3.5m. The operating performance for Alvis Moelv is disclosed separately in 2002 and 2003 as a business "to be discontinued". A summary of the exceptional items for 2002 and 2003, together with the 2004 charges detailed above, is as follows:

	2002 £m	2003 £m	2004 £m
Operating exceptionals			
Reorganisation following acquisition of Vickers Defence	2.0	2.0	3.5
Reduction in engineering manpower	–	–	1.5
Non-operating exceptionals			
Closure of Alvis Moelv	–	–	3.5
Other costs/(income) associated with previously divested business	–	(1.1)	–
	2.0	0.9	8.5

Interest

Net interest income declined from £2.1m in 2002 to £0.9m in 2003. While lower interest rates played a part in this reduction, the primary reason was lower average cash balances during the year. An increase in working capital on the main programmes at Alvis Hägglunds, albeit funded by customer advances, was the primary reason for this reduction. The first part of 2002 also benefited from higher cash balances before the outstanding convertible preference shares were redeemed in April 2002 for £31.5m.

Net interest income comprised £1.0m received by Alvis Hägglunds and £0.3m interest payable by Alvis South Africa. Despite a net cash position in the UK, interest income of £2.2m (2002: £1.8m) was offset by £1.3m of interest paid on the GKN loan note and £0.7m interest paid on the Lloyds loan (drawn in South African Rand). This is due to the interest rates applicable to the debt being considerably higher than those available for deposits.

Taxation

Due to a significant tax credit related to prior years, the Group's overall tax for the year was a credit of £0.1m (2002: charge of £4.5m), giving an effective rate of (0.5)% (2002: 31.0%).

Excluding goodwill and the prior year tax credit, the effective tax rate was 33.8% (2002: 34.4%). The adjusted tax rate is higher than the prevailing tax rates primarily due to losses in the Norwegian subsidiary which could not be offset against other profits in the Alvis Hägglunds' group.

The prior year tax credit of £6.5m (2002: £0.5m) consists of a number of items all of which relate to the UK. The largest item (£3.5m) relates to the capital gain on the disposal in 2001 of shares in Avimo. Due to a recent favourable change in legislation, the effective taxable gain has been reduced to nil. Additionally, in 2003 a number of outstanding matters were agreed with the Inland Revenue for which the Group had not previously taken any benefit through the profit and loss account. In cash terms, the prior year tax credit has been recouped through reduced payments to the Inland Revenue in 2003 and the receipt of a tax repayment of almost £3m in February 2004.

Earnings per share

Earnings per share were 19.3p after goodwill and exceptional items (2002: 9.1p). Before goodwill and exceptional items, earnings per share were 18.6p (2002: 10.4p). However, 2003 earnings benefited from the prior year tax credit of £6.5m. Excluding this tax item, earnings per share before goodwill and exceptional items on a current year tax basis were 12.5p (2002: 10.0p).

Cash and cash flow

At the year end, the Group had cash balances of £100.9m (2002: £87.0m) and net funds of £80.0m (2002: £65.3m). At the same time, the Group had total outstanding advances from customers of £131.0m (2002: £126.3m). In the balance sheet, the stock and debtors are shown after deducting customer advances on the contracts to which they relate. The balance of customer advances, which is disclosed within creditors, represents unapplied customer advances, totalling £38.3m (2002: £60.2m) at the year end. Deducting unapplied customer advances from net funds gives a balance of £41.7m (2002: £5.1m), which in the past we have referred to as "own" funds. The shortcoming of this method is that the customer advances are applied against related stock and debtor balances without considering the trade creditors associated with the contracts. To ignore trade creditors is to ignore an important element of the financing of the working capital of each programme, which in turn leads to an overstatement of the amount of customer advances being used to offset stock and debtors. Adjusting for this effect reduces "own" funds from £41.7m to £18.1m.

During the year, net funds including customer advances increased from £65.3m to £80.0m, representing a net inflow of £14.7m. £6.9m of the inflow arose on operating activities, where the operating profit before depreciation and amortisation (£24.2m) was offset by an increase in net working capital of £17.3m. The repayment to Alvis in respect of the working capital adjustment on the Vickers Defence acquisition resulted in a net funds inflow of £15.7m, while tax and dividends consumed £7.9m. Net interest received was £0.9m.

Net capital expenditure in the year was £6.2m, below the depreciation charge of £7.3m. £3.9m of the capital expenditure occurred in Sweden, where Alvis Hägglunds invested in machinery and infrastructure to support continued business growth.

Capital structure and funding

Shareholders' funds increased to £53.2m (2002: £33.3m). After dividends of £2.7m (2002: £6.8m), retained profits amounted to £17.7m, with the rest of the change in shareholders' funds attributable to the issue of ordinary shares and exchange.

Financing

During 2003, banking facilities in the UK, Sweden and South Africa were renewed but not significantly altered, except that the UK facilities are now available on an unsecured basis.

UK Group

Lloyds TSB provides Alvis plc and its UK subsidiaries with foreign exchange facilities, a £20m overdraft facility and an ancillary facility of up to £60m to support performance bonds and advance payment guarantees. These facilities are unsecured. The UK businesses also have access to a €12m bonding facility and foreign exchange facilities provided by the Royal Bank of Scotland.

At 31 December 2003, the UK working capital facilities were only utilised for forward foreign exchange contracts and bonding commitments (£26.9m). To minimise the cost of bonding at a time when the Group has cash resources, £20m has been placed on a deposit account to secure the bonding commitments. The Group intends to renew its UK facilities in early 2004.

As part of the acquisition of Vickers Defence, Alvis paid ZAR 71.7m (South African Rand) for a 75% interest in Alvis South Africa. This was funded by way of a ZAR 90m unsecured term loan facility, which attracts interest at 80 basis points over LIBOR and is repayable in instalments over 5 years. The average interest rate for 2003 on this facility was 13.1%.

Arising from the GKN Defence acquisition, GKN plc has provided funding by way of a £15m Unsecured Loan Note due September 2005, on which interest is payable at a fixed rate of 8.85%.

Sweden

Bank facilities continue to be provided to Alvis Hägglunds by Svenska Handelsbanken. These are primarily used to support guarantees and bonds issued by the company and, as at 31 December 2003, amounted to SEK 2,200m (£170.8m). This represents a small increase in the facility from SEK 2,020m to cover additional guarantee requirements arising from new business. Assets of Alvis Hägglunds have been partially used to secure these facilities together with a guarantee of approximately £20m from Alvis plc.

Alvis Hägglunds also has access to a facility for bonding commitments and foreign exchange dealing from SEB of approximately £25m. This facility, in common with the Svenska Handelsbanken facility, has covenants over net worth, interest cover and balance sheet gearing. In addition, some cash collateral for advance payment guarantees is required.

In conjunction with the banking facilities, a guarantee of £40m has been given by the Swedish Export Credits Guarantee Board (EKN) specifically in respect of the CV90 order from Switzerland.

South Africa

The capital structure of Alvis South Africa includes loans from the company's shareholders. At 31 December 2003, the loan from the 25% minority shareholder amounted to ZAR 15.0m (£1.3m). Additionally, Alvis South Africa has access to a local working capital facility from Nedbank of ZAR 50m (£4.2m). Alvis plc has guaranteed 75% of this facility and up to ZAR 60m of customer advances to Alvis South Africa from Armscor.

Treasury

The Group's Treasury function operates in line with policies approved by the Board. The primary objectives are:

- to manage foreign currency and interest rate exposures;
- to ensure the availability of facilities to finance new investment, working capital and guarantees; and
- to provide cash management.

Treasury instruments are only used to reduce risk and speculation is not permitted.

The Group is subject to two different exchange risks. Transaction risk arises on trading contracts upon which sums may be receivable or payable in foreign currencies. To reduce this risk, the policy is to hedge such exposures upon contract award.

Translation risk arises on the translation of both earnings and net assets of foreign subsidiaries. Because of the potential short term volatility of the Swedish Krona versus sterling, the Board has implemented a policy of permitting part of Alvis Hägglunds' budgeted profits to be hedged when market conditions permit.

With respect to the translation of the net assets of foreign subsidiaries, the Board considers that foreign subsidiaries are long term investments and over time foreign exchange rates tend to be stable (other than in hyper-inflationary environments). In these circumstances, there should be no requirement to hedge the net assets of foreign subsidiaries.

The Board also recognises, however, that on occasion a natural hedge may exist, for example by using foreign denominated borrowings. In these circumstances it is appropriate to designate such an instrument as a hedge against an investment in a foreign subsidiary. The natural hedge must have a commercial rationale and not be for the sole purpose of creating a hedge.

The Alvis Group no longer has an outstanding Krona denominated loan. As a result, Alvis Hägglunds' net assets of SEK 717m (£55.7m) were unhedged at the year end.

A translation adjustment of £3.2m is included in shareholders' funds, which represents the exchange gain on Alvis Hägglunds' net assets arising from the strengthening of the Krona from 14.0: £1 last year to 12.9: £1 at 31 December 2003.

At 31st December 2003, Alvis had an exposure to 75% of the net assets of Alvis South Africa, amounting to ZAR 73.5m (£6.2m) including shareholder loans, compared to a borrowing in the UK of ZAR 52.5m (£4.4m).

The Board has a conservative policy towards the investment of surplus cash, with the protection of principal being the main objective. Its guidelines require that cash should be invested with a number of different institutions, each having where possible AA long term rating, and on fixed deposit maturity not exceeding 6 months.

The Group endeavours to maximise the rate of return on its cash resources within the policies outlined above. To this end, the Group has continued its use of International Money Market Funds for overnight cash deposits. These AAA investments have proved successful in providing a higher return than alternative overnight deposits whilst retaining flexibility and capital protection.

Reporting Standards

From 1 January 2005, Alvis plc will be required to prepare its consolidated financial statements in accordance with International Financial Reporting Standards (IFRS). From Alvis's perspective, the main differences between these standards and those currently adopted arise in the accounting treatment for hedges, share option costs, pensions and development costs. It is not yet possible to quantify the impact of IFRS, largely due to the infancy of many of the standards which will apply on adoption, although preparation is underway to ensure that our business processes, systems and policies are able to meet any revised requirements of IFRS.

Martin Greenslade
Finance Director

Group Profit and Loss Account

Year ended 31 December 2003

	Notes	Year ended 31 December 2003 £000	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000	Year ended 31 December 2002 £000
Turnover	1				
Continuing operations, including joint ventures		354,050		225,858	
Share of turnover of continuing joint ventures		(13,761)		(7,798)	
Ongoing operations			340,289		218,060
Operations to be discontinued			8,554		7,654
Continuing operations			348,843		225,714
Cost of sales	2		(292,351)		(183,456)
Gross profit			56,492		42,258
Administration expenses before operating exceptional items	2		(36,260)		(27,861)
Trading profit/(loss) before operating exceptional items					
Ongoing operations		22,539		15,647	
Operations to be discontinued		(2,307)		(1,250)	
Continuing operations			20,232		14,397
Operating exceptional items in respect of ongoing operations	3		(1,995)		(2,048)
Total administration expenses			(38,255)		(29,909)
Trading profit/(loss)					
Ongoing operations		20,544		13,599	
Operations to be discontinued		(2,307)		(1,250)	
Continuing operations			18,237		12,349
Share of results of continuing joint ventures			21		15
Operating Profit	5		18,258		12,364
Non-operating exceptional items:	7				
Continuing operations			36		71
Discontinued operations			1,049		–
Profit on ordinary activities before interest			19,343		12,435
Net interest receivable	8		920		2,108
Profit on ordinary activities before taxation			20,263		14,543
Taxation	9		104		(4,515)
Profit on ordinary activities after taxation			20,367		10,028
Equity minority interests			32		42
Profit attributable to shareholders	10		20,399		10,070
Dividends, including non-equity shares	11		(2,660)		(6,809)
Transfer to reserves	26		17,739		3,261
Basic earnings per ordinary share before exceptional items and goodwill	12		18.6p		10.4p
Basic earnings per ordinary share	12		19.3p		9.1p
Diluted earnings per ordinary share before exceptional items and goodwill	12		17.7p		9.9p
Diluted earnings per ordinary share	12		18.4p		8.6p

At 31 December 2003

	Notes	Group at 31 December 2003 £000	Group at 31 December 2002 £000	Company at 31 December 2003 £000	Company at 31 December 2002 £000
Fixed assets					
Intangible assets:	13				
(Negative goodwill)/goodwill		**(663)**	255	**–**	–
Tangible assets	14	**50,274**	49,266	**1,200**	1,285
Investments					
Interest in assets of joint ventures		**6,738**	3,093	**–**	–
Interest in liabilities of joint ventures		**(6,641)**	(3,018)	**–**	–
		97	75	**–**	–
Investment in associates		**32**	30	**–**	–
Other investments		**–**	–	**103,577**	103,577
Total investments	15	**129**	105	**103,577**	103,577
		49,740	49,626	**104,777**	104,862
Current assets					
Stocks	16	**51,486**	38,148	**–**	–
Debtors due within one year	17	**36,695**	59,622	**90,954**	105,492
Debtors due after one year	17	**2,997**	5,734	**132**	121
Cash at bank and in hand		**100,862**	88,336	**61,680**	13,736
		192,040	191,840	**152,766**	119,349
Creditors due within one year	18	**(113,855)**	(137,377)	**(100,750)**	(74,228)
Net current assets		**78,185**	54,463	**52,016**	45,121
Total assets less current liabilities		**127,925**	104,089	**156,793**	149,983
Creditors due after one year	19	**(40,887)**	(37,860)	**(18,827)**	(19,702)
Provisions for liabilities and charges	24	**(33,790)**	(32,918)	**(25)**	(5)
Equity minority interests		**(49)**	(3)	**–**	–
Net assets employed		**53,199**	33,308	**137,941**	130,276
Capital and reserves					
Called up share capital	25	**27,570**	27,265	**27,570**	27,265
Share premium account	26	**2,006**	1,164	**2,006**	1,164
Capital redemption reserve	26	**37,014**	37,014	**37,014**	37,014
Own shares held in trust	26	**(4,788)**	(5,533)	**(4,788)**	(5,533)
Profit and loss account	26	**(8,603)**	(26,602)	**76,139**	70,366
Equity shareholders' funds		**53,199**	33,308	**137,941**	130,276

These accounts were approved by the Board on 10 March 2004.

N M Prest

M F Greenslade

Group Statement of Total Recognised Gains and Losses

Year ended 31 December 2003

	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000
Profit attributable to shareholders, excluding share of profits of joint ventures	**20,382**	10,066
Share of joint ventures' profit for the year	**17**	4
Profit attributable to shareholders	**20,399**	10,070
Exchange difference on retranslation of net assets of subsidiaries	**1,076**	2,660
Exchange difference on loans drawn down for acquisition of subsidiaries	**(806)**	(211)
Other recognised gains and losses relating to the year (exchange)	**32**	75
Total recognised gains and losses relating to the year	**20,701**	12,594

Group Reconciliation of Movement in Shareholders' Funds

Year ended 31 December 2003

	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000
Profit attributable to shareholders	**20,399**	10,070
Dividends	**(2,660)**	(6,809)
	17,739	3,261
Issue of new shares	**1,147**	595
Redemption of Convertible Cumulative Non-Voting Redeemable Preference shares	**–**	(31,462)
Other recognised gains and losses relating to the year (exchange)	**302**	2,524
Purchase of own shares held in trust	**–**	(584)
Disposal of own shares held in trust	**745**	457
Movement in respect of recognition of costs of options over ordinary shares	**(42)**	77
Net increase/(decrease) in shareholders' funds	**19,891**	(25,132)
Shareholders' funds at beginning of the year	**33,308**	58,440
Shareholders' funds at end of the year	**53,199**	33,308

The opening shareholders' funds at 1 January 2003 have been restated in accordance with the change in accounting for own shares held in trust. The effect was a reduction in shareholders' funds of £5,330,000 from £38,638,000 to £33,308,000 (note 26).

	Notes	Year ended 31 December 2003 £000	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000	Year ended 31 December 2002 £000
Net cash inflow/(outflow) from operating activities	30 (a)		**6,919**		(16,076)
Returns on investments and servicing of finance					
Interest received		**4,375**		4,065	
Interest paid		**(3,483)**		(1,313)	
Interest element of finance lease payments		**(10)**		(8)	
Dividends paid on preference shares		**–**		(969)	
			882		1,775
Taxation					
Paid		**(3,251)**		(6,171)	
Received		**1,905**		189	
			(1,346)		(5,982)
Capital expenditure and financial investment					
Purchase of tangible fixed assets	14	**(6,363)**		(5,570)	
Sale of tangible fixed assets		**125**		170	
			(6,238)		(5,400)
Acquisitions and disposals					
Acquisition of Vickers Defence	30 (c)	**15,684**		(17,972)	
Net overdraft acquired with Vickers Defence	30 (c)	**–**		(1,252)	
Disposal of shares in associates		**–**		269	
Costs related to previously disposed of subsidiaries		**(98)**		–	
			15,586		(18,955)
Dividends paid on ordinary shares			**(6,533)**		(5,941)
Management of liquid resources*					
Funds placed on time deposit		**(18,561)**		(8,666)	
Maturities of time deposits		**38,196**		86,483	
Decrease in funds on deposit			**19,635**		77,817
Financing					
Issue of shares		**1,147**		594	
Net change in own shares held in trust		**745**		(127)	
Redemption of £1 convertible preference shares		**–**		(31,462)	
(Decrease)/increase in debt and lease financing		**(1,789)**		5,274	
			103		(25,721)
Increase in cash in the year			**29,008**		1,517
Reconciliation of net cash flow to movement in net funds	30 (b)				
Increase in cash in the year		**29,008**		1,517	
Add back/(deduct):					
Repayment/(drawdown) of debt and lease financing		**1,789**		(5,274)	
Cash taken off short term deposits		**(19,635)**		(77,817)	
Change in net funds resulting from cash flows			**11,162**		(81,574)
Exchange differences			**3,507**		5,258
Net funds at beginning of the year			**65,335**		141,651
Net funds at end of the year			**80,004**		65,335

* Liquid resources comprise solely term deposits which do not have a maturity exceeding 6 months.

Accounting convention

The accounts have been prepared in accordance with applicable accounting standards using the historical cost convention.

Basis of consolidation

The Group accounts include the accounts of the holding company and its subsidiary undertakings ("subsidiaries") made up to 31 December 2003, together with the appropriate proportions of the results and net assets of associated undertakings ("associates") and joint venture undertakings ("joint ventures").

The results of subsidiaries, associates and joint ventures acquired or disposed of during the year are included from or to the effective date of acquisition or disposal.

It was announced on 29 January 2004 that the Group would close its Norwegian business, Alvis Moelv AS, during 2004. The operating results of Alvis Moelv have been disclosed within continuing operations as 'to be discontinued' for the year ended 31 December 2003 and comparatives for 2002 have been restated accordingly. Under accounting standards, the closure costs have not been recognised in the year ended 31 December 2003.

The results of the Group's joint ventures are included in accordance with the gross equity method.

Goodwill

The excess of the cost of acquiring subsidiaries, associates and joint ventures over the fair value of the related net assets acquired is goodwill. In accordance with Financial Reporting Standard 10, the goodwill arising on or after 23 December 1998 is capitalised in the balance sheet as an intangible fixed asset. Where goodwill arises on an acquisition by an associate or joint venture of the Group, the goodwill is capitalised as part of the equity value of the associate/joint venture and disclosed within fixed asset investments. Capitalised goodwill is amortised through the profit and loss account over its estimated useful economic life, up to a maximum of twenty years.

Negative goodwill arises where the cost of acquiring subsidiaries, associates and joint ventures is less than the fair value of the net assets acquired. Negative goodwill is capitalised in the balance sheet as an intangible asset, immediately after positive goodwill. Capitalised negative goodwill is amortised through the profit and loss account, as part of operating profit, over the estimated life of the non-monetary assets (including stock) acquired and specific events or contracts which contributed to the negative goodwill.

Goodwill arising on acquisitions prior to 23 December 1998 was taken directly to reserves and has been offset against the retained profit and loss account of the Group.

On the disposal of a business, unamortised goodwill remaining in the balance sheet as an intangible asset or as part of the equity investment of an associate/joint venture or goodwill previously taken directly to reserves is charged to the profit and loss account.

Group turnover

Turnover represents the amounts invoiced by the Group in respect of goods and services provided during the year at agreed or provisional prices, excluding sales between Group undertakings.

Turnover includes a prudent assessment of the value of the work performed on major long term contracts.

Tangible fixed assets

Tangible fixed assets are included at cost. Depreciation is provided on a straight line basis so as to write off the assets over their estimated useful lives mainly at the following rates:

Freehold land	Nil
Freehold and long leasehold buildings	2%
Short leasehold buildings	Term of lease
Plant, machinery and fixtures	10% - 25%

Leasing

Certain items of plant and equipment are financed by leasing arrangements which give rights that approximate to ownership. These are included in the balance sheet as fixed assets at cost less depreciation and the interest element is charged in the profit and loss account over the period of the lease in proportion to the balance of capital repayments outstanding. The costs of operating leases are charged on a straight line basis over the lease term.

Research and development

Expenditure recoverable under customer funded design and development contracts is included in work in progress. Expenditure on the development of specific products is carried forward as an intangible fixed asset when its recoverability can be foreseen with reasonable assurance, and is amortised in line with the future life of the product. Research and general development expenditure not recoverable under contract is written off in the year in which it is incurred.

Stocks

Stocks are valued at the lower of cost and net realisable value, less any foreseeable losses and payments received on account. Cost comprises prime costs of direct labour and materials together with attributable production overheads.

Major contracts of a duration in excess of one year are classified as long term contracts. A prudent assessment of work performed on major long term contracts, valued at cost plus attributable profit, is included in debtors, net of related progress payments. Payments on account received from customers in excess of the work in progress value of the related contract are shown as advance receipts within creditors.

Pensions

The Group currently accounts for pension costs in accordance with the requirements of Statement of Standard Accounting Practice (SSAP) 24.

Additional disclosures in accordance with Financial Reporting Standard (FRS) 17 Retirements Benefits have been made in the Notes to the Accounts.

During the course of the year, the Group operated a defined benefit pension scheme in the UK, namely the Alvis Pension Scheme. Contributions to the scheme are made by employees and Group companies.

The assets of the scheme are held in trust separate from the Group's finances and are managed by external professional fund managers. An independent valuation is carried out at least every three years. The expected regular cost of providing retirement benefits is assessed by external professional actuaries and attributed to individual years using the projected unit method. Variations in pension cost arising from subsequent actuarial valuations are amortised over the remaining service lives of the employees concerned, assumed to be 15 years.

Overseas, the Group operates a number of pension plans, both on a defined contribution and defined benefit basis. The amount charged to the profit and loss account for defined contribution schemes is the contribution payable for the period. For funded defined benefit schemes, the levels of contribution are determined by independent third parties and charged to the profit and loss account as incurred. For the unfunded element of the multi-employer defined benefit scheme in Sweden, the liability is determined by an independent actuary and is recorded in the balance sheet. The movement in the liability for the period is charged to the profit and loss account.

Taxation

Deferred tax is recognised in respect of all timing differences that have arisen but not reversed at the balance sheet date where transactions or events have occurred at that date that will result in an obligation to pay more, or a right to pay less or to receive more, tax, with the following exceptions:

- provision is only made for tax on gains arising from the revaluation (and similar fair value adjustments) of fixed assets, and gains on disposal of fixed assets that have been rolled over into replacement assets, to the extent that, at the balance sheet date, there is a binding agreement to dispose of the assets concerned. However, no provision is made where, on the basis of all available evidence at the balance sheet date, it is more likely than not that the taxable gain will be rolled over into replacement assets:
- deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted:
- provision is made for deferred tax that would arise on remittance of the retained earnings of overseas subsidiaries, associates and joint ventures only to the extent that, at the balance sheet date, dividends have been accrued as receivable.

Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

Foreign currencies

Transactions in foreign currencies are recorded at the rate of exchange ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated at the exchange rate ruling on the balance sheet date or, if appropriate, at a forward exchange contract rate. Profits and losses of subsidiaries, branches, associates and joint ventures which have currencies of operation other than sterling are translated into sterling at average rates of exchange except for material transactions which are translated at the rate ruling on the date of transaction.

Exchange differences arising from the retranslation of the opening net assets of subsidiaries, branches, associates and joint ventures which have currencies of operation other than sterling and any related loans designated as a hedge are taken to reserves together with the differences arising between the profit and loss accounts translated at average or actual rates and the rates ruling at the year end. Other exchange differences are taken to the profit and loss account.

Derivative financial instruments

The Group uses derivative financial instruments to hedge its exposure to fluctuations in foreign exchange rates.

Where the Group has entered into a forward contract to reduce or eliminate a foreign currency exposure on a future transaction arising from a contracted commitment, the hedged item is accounted for using the forward exchange rate.

Share options

In accordance with Urgent Issues Task Force Abstract 25, National Insurance Contributions on Share Option Gains, the Group provides for the employer's national insurance liability over the vesting period of the options by reference to the year end mid-market price of the ordinary shares of the Company. The cost is charged as part of the operating profit in the profit and loss account.

In accordance with Urgent Issues Task Force Abstract 17, Employee Share Schemes, the Group charges the discount between the option price and market value on grant date. The cost is charged as part of the operating profit, in the profit and loss account, over the vesting period of the option with the accrual credited to shareholders' funds. The Group has taken advantage of the exemption offered in Urgent Issues Task Force Abstract 17 from charging to the profit and loss account the discount in respect of approved employee SAYE schemes.

Own shares held in trust

In accordance with Urgent Issues Task Force Abstract 38, Accounting for ESOP Trusts, the Group discloses the investment in own shares (held within the Alvis Employee Benefit Trust) as a deduction from shareholders' funds. Previously, own shares were disclosed within fixed assets as an investment. Comparatives have been restated accordingly.

Urgent Issues Task Force Abstract 38 has also been applied for the Company, Alvis plc, as the sponsoring company of the Alvis Employee Benefit Trust.

1 Turnover, operating profit and net assets

a) Turnover by destination:

	Year ended 31 December 2003			Year ended 31 December 2002		
	Ongoing operations	**Operations to be discontinued**	**Continuing operations**	Ongoing operations	Operations to be discontinued	Continuing operations
	£000	**£000**	**£000**	£000	£000	£000
United Kingdom	**127,618**	**3,711**	**131,329**	43,919	2,353	46,272
Rest of Europe	**177,493**	**4,821**	**182,314**	111,441	5,173	116,614
North America	**1,145**	**22**	**1,167**	845	128	973
South America	**31**	**–**	**31**	48	–	48
Africa	**29,173**	**–**	**29,173**	6,771	–	6,771
Asia	**18,211**	**–**	**18,211**	62,723	–	62,723
Australasia	**379**	**–**	**379**	111	–	111
	354,050	**8,554**	**362,604**	225,858	7,654	233,512

Turnover for the years ended 31 December 2003 and 2002 is all in respect of specialist vehicles activity.
Turnover of continuing operations to the Rest of Europe includes the Group's share of turnover of continuing joint venture operations of £13,761,000 (2002: £7,798,000).

b) By origin and activity:
Year ended 31 December 2003

	Turnover	**Operating profit/(loss)**	**Net assets**
	£000	**£000**	**£000**
Ongoing operations:			
United Kingdom	**136,591**	**4,778**	**(15,644)**
Rest of Europe	**177,470**	**19,639**	**18,028**
South Africa	**30,783**	**224**	**8,252**
	344,844	**24,641**	**10,636**
Operations to be discontinued :			
Rest of Europe	**8,554**	**(2,307)**	**3,035**
Exclude continuing operation turnover between geographical segments:			
United Kingdom sales to Rest of Europe	**(2,025)**		
United Kingdom sales to South Africa	**(12)**		
Rest of Europe sales to United Kingdom	**(1,790)**		
Rest of Europe sales to South Africa	**(16)**		
South Africa sales to Rest of Europe	**(21)**		
Exclude operation to be discontinued turnover between geographical segments:			
United Kingdom sales to Rest of Europe	**(691)**		
	348,843	**22,334**	**13,671**
Unallocated	**–**	**(2,102)**	**39,399**
		20,232	
Operating exceptionals (in respect of United Kingdom)		**(1,995)**	**–**
Continuing joint ventures	**13,761**	**21**	**97**
Continuing associates		**–**	**32**
	362,604	**18,258**	**53,199**

All of the above are in respect of continuing operations. The operating profit of continuing operations includes negative goodwill amortisation of £1,386,000. The operating profit of the United Kingdom operations is after crediting £1,934,000 of negative goodwill amortisation.

b) By origin and activity:

Year ended 31 December 2002

	Turnover £000	Operating profit/(loss) £000	Net assets £000
Ongoing operations:			
United Kingdom	107,459	4,920	(12,687)
Rest of Europe	104,064	12,403	25,643
South Africa	6,793	75	8,529
	218,316	17,398	21,485
Operations to be discontinued:			
Rest of Europe	7,654	(1,250)	9,330
Exclude continuing operation turnover between geographical segments:			
United Kingdom sales to Rest of Europe	(30)		
South Africa sales to United Kingdom	(226)		
	225,714	16,148	30,815
Unallocated	–	(1,751)	2,388
		14,397	
Operating exceptionals (in respect of United Kingdom)		(2,048)	–
Continuing joint ventures	7,798	15	75
Continuing associates		–	30
	233,512	12,364	33,308

All of the above are in respect of continuing operations. Operating profit of continuing operations includes goodwill amortisation of £2,000.

Unallocated costs comprise head office costs and consolidation adjustments. Unallocated net assets comprise non-operating and interest bearing assets and liabilities which include the Group's cash, advance receipts and loans.

2 Cost of sales and administration expenses before operating exceptional items

	Ongoing operations	**Operations to be discontinued**	**Continuing operations**
Year ended 31 December 2003	**£000**	**£000**	**£000**
Cost of sales	**282,771**	**9,580**	**292,351**
Administration expenses before operating exceptional items	**35,177**	**1,083**	**36,260**
Year ended 31 December 2002			
Cost of sales	176,080	7,376	183,456
Administration expenses before operating exceptional items	26,333	1,528	27,861

All of the above are in respect of specialist vehicles activity. The administration expenses of continuing operations are net of negative goodwill amortisation of £1,386,000 (2002: £2,000 goodwill amortisation). The total administration expenses as disclosed in the Group profit and loss account (page 22) are after including the operating exceptional items (note 3).

3 Operating exceptional items

During the year ended 31 December 2003, £1,995,000 was charged (2002: £2,048,000) in respect of reorganisation at Alvis Vickers following the acquisition of Vickers Defence on 30 September 2002. This charge was all in respect of ongoing operations.

4 Staff costs

a) Staff costs (including Executive Directors):

	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000
Wages and salaries	**64,780**	41,436
Social security costs	**11,497**	8,155
Other pension costs (note 28)	**5,752**	3,144
	82,029	52,735

b) Average number of employees:

	Number	Number
Production	**2,213**	1,407
Selling and administration	**591**	476
	2,804	1,883

Details for each Director's remuneration, pension entitlements and interest in the issued share capital and share options are shown in the Remuneration Report.

5 Operating profit

	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000
Operating profit is stated after charging/(crediting) the following:		
(Negative goodwill)/goodwill amortisation	**(1,386)**	2
Depreciation of tangible fixed assets		
- owned	**7,258**	5,409
- leased	**79**	146
Operating lease rentals		
- plant	**435**	582
- other	**1,469**	980
Auditors' remuneration (note 6)		
- audit fees – UK	**218**	184
- audit fees – overseas	**82**	50
- non-audit fees – UK	**17**	8
- non-audit fees – overseas	**17**	30
Private venture research and development	**6,056**	5,446

6 Auditors' remuneration

	Year ended 31 December 2003			Year ended 31 December 2002		
	UK	**Overseas**	**Total**	UK	Overseas	Total
	£000	**£000**	**£000**	£000	£000	£000
Audit services						
Statutory audit fee	**218**	**82**	**300**	184	50	234
Other assurance services	**8**	**4**	**12**	8	–	8
	226	**86**	**312**	192	50	242
Further assurance services						
Due diligence work in respect of the acquisition of Vickers OMC (part of Vickers Defence)	–	–	–	49	–	49
Working capital report in respect of the acquisition of Vickers Defence	–	–	–	185	–	185
	–	–	–	234	–	234
Tax services						
Compliance services	–	**1**	**1**	–	3	3
Advisory services	**6**	**8**	**14**	–	4	4
	6	**9**	**15**	–	7	7
Other services						
Assistance in respect of commercial contracts	–	–	–	–	5	5
Pensions	**3**	–	**3**	–	4	4
Other	–	**4**	**4**	–	14	14
	3	**4**	**7**	–	23	23
Total	**235**	**99**	**334**	426	80	506
The above remuneration was charged as follows:						
Within operating profit (note 5)	**235**	**99**	**334**	192	80	272
Within goodwill on the acquisition of Vickers Defence	–	–	–	234	–	234
	235	**99**	**334**	426	80	506

All of the above amounts related to services provided by Ernst & Young LLP. Included within the UK total above are fees incurred by the Company of £112,000 (2002: £317,000, including £234,000 in respect of the acquisition of Vickers Defence). The policy in respect of the auditors is discussed within the Corporate Governance Report (page 64).

Explanation for engaging auditors on significant non-audit services

During the year ended 31 December 2002, Ernst & Young LLP were engaged in relation to the acquisition of Vickers Defence to confirm the existence of adequate working capital facilities within the enlarged group. It is a requirement that the circular issued to shareholders in connection with the acquisition contained such a confirmation by a firm of accountants. Ernst & Young LLP were chosen for this work due to their existing knowledge of the systems, business issues and forecasting processes of the Alvis Group.

Alongside this working capital review in South Africa, Ernst & Young LLP conducted a due diligence review of Vickers OMC. The choice of Ernst & Young LLP avoided duplicated work and provided a review of the business independent from the incumbent auditors.

Fees to accounting firms other than Ernst & Young LLP for non-audit services amounted to £124,116 in 2003 (2002: £111,741 of which £89,561 was in respect of the acquisition of Vickers Defence).

7 Non-operating exceptional items

	Year ended 31 December 2003 £000	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000	Year ended 31 December 2002 £000
Continuing operations:				
Profit on disposal of fixed assets	**36**		71	
		36		71
Discontinued operations:				
Recognition of deferred consideration on the disposal of Barracuda Technologies AB	**1,147**		–	
Costs in respect of previously divested businesses	**(98)**		–	
		1,049		–
		1,085		71

8 Net interest receivable

	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000
Interest payable on:		
Bank loans and overdrafts	**(825)**	(232)
Other loans	**(1,530)**	(1,361)
Finance charges payable under finance leases	**(10)**	(8)
	(2,365)	(1,601)
Interest receivable	**3,279**	3,705
Net group interest receivable	**914**	2,104
Net joint venture interest receivable	**6**	4
Net interest receivable	**920**	2,108

9 Taxation

	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000
The taxation (credit)/charge based on the results for the year is analysed as follows:		
Current tax:		
UK Corporation tax for the current year	**3,768**	2,881
Double Taxation Relief	**(2,162)**	–
Overseas tax for the current year	**4,005**	2,822
	5,611	5,703
UK Corporation tax for prior years	**(6,535)**	(648)
Overseas tax for the prior year	**–**	34
	(6,535)	(614)
Total current tax	**(924)**	5,089
Deferred tax:		
UK deferred tax for the current year	**(694)**	(1,362)
Overseas deferred tax for current year	**1,444**	643
	750	(719)
UK deferred tax for prior years	**60**	130
Total deferred tax	**810**	(589)
Share of joint ventures' tax	**10**	15
	(104)	4,515

9 Taxation (continued)

The effective tax rate for the Group is a credit of just under 1% (2002: tax charge rate of 31%). The Group's standard rate for current tax for year ended 31 December 2003 is 28.3% charge (2002: 28.5% charge), based upon the weighted average of profits before tax. This is based upon the following standard rates of taxation.

	2003	2002
	%	%
UK	**30**	30
Sweden	**28**	28
South Africa	**30**	30

The current tax credit (2002: charge) for the period is below the Group's standard rate for the reasons set out below:

	Year ended 31 December 2003	Year ended 31 December 2002
	£000	£000
Profit before tax	**20,263**	14,543
Tax on ordinary profit at Group standard rate	**5,739**	4,150
Factors affecting charge:		
Disallowable expenses	**957**	306
Non-taxable negative goodwill	**(548)**	–
Capital allowances in excess of depreciation for the year	**(330)**	(599)
Losses arising in current year not recognised	**237**	500
Deferred tax previously provided on intragroup gain	**–**	1,252
Swedish statutory taxation reserve	**(698)**	(517)
Other short term timing differences	**237**	601
Prior year movements	**(6,535)**	(614)
Other	**17**	10
Current tax charge for the year	**(924)**	5,089

Included within the taxation charge above is a non-operating exceptional tax charge of £304,000 (2002: charge of £22,000) and also an operating exceptional tax credit in respect of the reorganisation costs charged within Alvis Vickers of £599,000 (2002: £614,000).

Factors that may affect future tax charges:

The Group will benefit from the tax effect of Research and Development credits in the UK, thereby reducing the current tax rate. No provision has yet been made for the effect of these credits.

The Group's Norwegian operation has generated losses in the past. The utilisation of these losses is unlikely following announcement of closure of the operation. A deferred tax asset in respect of the losses has therefore not been recognised.

No provision has been made for deferred taxation on gains recognised on the sale of properties where potentially taxable gains have been rolled over into replacement assets. The total amount unprovided is £2.2m (2002: £2.2m). Such tax would only become payable if the replacement assets were sold. At present it is not envisaged that any tax will become payable.

10 Profit attributable to shareholders

As permitted by section 230(1) of the Companies Act 1985, the Company has not presented its own profit and loss account as part of these accounts. The Group profit attributable to shareholders for the year ended 31 December 2003 includes a profit of £5,815,000 (2002: £2,364,000) which has been dealt with in the accounts of the Company.

11 Dividends

	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000
Ordinary shares		
Interim: 2.5p per share (2002: 2.3p)	**2,660**	2,399
Proposed final: nil pence per share (2002: 3.7p)	**–**	3,873
Total: 2.5p per share (2002: 6.0p)	**2,660**	6,272
Preference shares		
Convertible preference dividend paid	**–**	537
	2,660	6,809

The Alvis Employee Benefit Trust waived its right to dividends paid and declared on ordinary shares during both years.

12 Earnings per ordinary share

	Profit for the year		Weighted average number of shares		Earnings per share	
	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000	**Year ended 31 December 2003 number**	Year ended 31 December 2002 number	**Year ended 31 December 2003 pence**	Year ended 31 December 2002 pence
Basic earnings per share before all exceptional items and goodwill	**19,628**	10,920	**105,618,458**	104,212,752	**18.6**	10.4
Operating exceptional items	**(1,995)**	(2,048)				
Tax on operating exceptional items	**599**	614				
Non-operating exceptional items	**1,085**	71				
Tax on non-operating exceptional items	**(304)**	(22)				
Goodwill amortisation	**1,386**	(2)				
Basic earnings per share	**20,399**	9,533	**105,618,458**	104,212,752	**19.3**	9.1
Effect of dilutive securities:						
Employee share option schemes			**1,349,868**	1,459,045		
Alvis Employee Benefit Trust			**3,642,440**	4,444,463		
Diluted earnings per share	**20,399**	9,533	**110,610,766**	110,116,260	**18.4**	8.6
Operating exceptional items	**1,995**	2,048				
Tax on operating exceptional items	**(599)**	(614)				
Non-operating exceptional items	**(1,085)**	(71)				
Tax on non-operating exceptional items	**304**	22				
Goodwill amortisation	**(1,386)**	2				
Diluted earnings per share before all exceptional items and goodwill	**19,628**	10,920	**110,610,766**	110,116,260	**17.7**	9.9

The calculation of the basic earnings per share is based upon profit attributable to shareholders of £20,399,000 (2002: £10,070,000) less convertible preference dividends of £nil (2002: £537,000).

12 Earnings per ordinary share (continued)

The earnings per ordinary share before all exceptional items (including the reorganisation costs at Alvis Vickers Limited) and goodwill have been calculated in addition to the earnings per ordinary share required by Financial Reporting Standard 14 as, in the opinion of the Directors, this will allow shareholders to consider the results of the Group on a comparable basis.

In calculating the basic earnings per ordinary share the weighted average number of shares in issue excludes the shares held by the Alvis Employee Benefit Trust at 31 December 2003 of 3,642,440 (2002: 4,444,463).

The convertible preference shares were fully redeemed in 2002 and are no longer relevant to the diluted earnings per share calculation.

13 Intangible assets

During the year ended 31 December 2002, goodwill arising on the acquisition of Vickers Defence was £257,000. As at 31 December 2002, the net book value of the goodwill was £255,000 after goodwill amortisation charged to the profit and loss account (note 5) in the last quarter of 2002 of £2,000. It was stated in the 2002 Annual Report that the calculation of goodwill included estimated fair values. The fair values have now been finalised (note 30(c)), resulting in an adjustment to the goodwill of £2,304,000, resulting in negative goodwill of £2,047,000. During the year ended 31 December 2003, £1,386,000 of negative goodwill amortisation has been credited to the profit and loss account as part of the operating profit (note 5) resulting in cumulative negative goodwill amortisation of £1,384,000. The net book value of negative goodwill at 31 December 2003 of £663,000 is to be amortised to the profit and loss account over the next three years, with the majority being credited in 2004. The amortisation of negative goodwill to the profit and loss account is in line with the expected realisation of the acquired stock and fixed assets and specific events or contracts which contributed to the negative goodwill.

14 Tangible fixed assets

Group	Freehold land and buildings £000	Long leasehold land and buildings £000	Short leasehold land and buildings £000	Plant machinery and fixtures £000	Total £000
Cost					
At 31 December 2002	36,736	1,307	–	36,537	74,580
Additions	810	–	637	4,916	6,363
Disposals	(8)	–	–	(630)	(638)
Exchange	1,685	–	–	1,515	3,200
At 31 December 2003	**39,223**	**1,307**	**637**	**42,338**	**83,505**
Depreciation					
At 31 December 2002	(5,264)	(137)	–	(19,913)	(25,314)
Charge for the year	(1,759)	(26)	–	(5,552)	(7,337)
Eliminated on disposals	–	–	–	549	549
Exchange	(327)	–	–	(802)	(1,129)
At 31 December 2003	**(7,350)**	**(163)**	**–**	**(25,718)**	**(33,231)**
Net book values					
At 31 December 2003	**31,873**	**1,144**	**637**	**16,620**	**50,274**
At 31 December 2002	31,472	1,170	–	16,624	49,266

14 Tangible fixed assets (continued)

Included within fixed assets are plant, machinery and fixtures held under finance leases and hire purchase agreements. The cost of these assets is £261,000 (2002: £311,000) with accumulated depreciation charged of £53,000 (2002: £150,000).

Company	Long leasehold land and buildings £000	Plant machinery and fixtures £000	Total £000
Cost			
At 31 December 2002	1,307	682	1,989
Additions	–	22	22
Disposals	–	(137)	(137)
At 31 December 2003	**1,307**	**567**	**1,874**
Depreciation			
At 31 December 2002	(137)	(567)	(704)
Charge for the year	(26)	(49)	(75)
Eliminated on disposals	–	105	105
At 31 December 2003	**(163)**	**(511)**	**(674)**
Net book values			
At 31 December 2003	**1,144**	**56**	**1,200**
At 31 December 2002	1,170	115	1,285

Group capital expenditure authorisations	At 31 December 2003 £000	At 31 December 2002 £000
Contracted	**441**	204

15 Investments

	Group 31 December 2003 £000	Group 31 December 2002 £000	**Company 31 December 2003 £000**	Company 31 December 2002 £000
Subsidiaries	–	–	**103,577**	103,577
Associates	**32**	30	–	–
Joint ventures	**97**	75	–	–
	129	105	**103,577**	103,577

	Group Associates	Group Joint ventures	Group Total	Company Total
Analysis of movements in the year:	£000	£000	£000	£000
At 31 December 2002	30	75	105	103,577
Other net movements (exchange)	2	5	7	–
Share of retained profit for the year	–	17	17	–
At 31 December 2003	**32**	**97**	**129**	**103,577**

The principal Alvis Group trading undertakings are shown on the inside back cover of the 2003 Annual Report, together with their country of incorporation. The nature of their businesses is described within the Company Information on page 2 of this report. They are all 100% indirectly held subsidiaries of the Company with the exception of Alvis South Africa (Pty) Limited which is a 75% indirectly held subsidiary.

Principal joint ventures as at 31 December 2003 were as follows:

	Country of incorporation	% of ordinary share capital held by group	Nature of business
ARTEC	Germany	33.3	Development of MRAV
Patria Hägglunds Oy	Finland	50.0	Supply of armoured vehicles

There were no principal associates as at 31 December 2003 or 31 December 2002.

16 Stocks

	Group 31 December 2003 £000	Group 31 December 2002 £000
Raw materials and consumables	**26,610**	25,187
Work in progress	**76,206**	49,534
Finished goods	**17,411**	8,128
	120,227	82,849
Payments on account	**(68,741)**	(44,701)
	51,486	38,148

17 Debtors

	Group 31 December 2003	Group 31 December 2002	Company 31 December 2003	Company 31 December 2002
Due within one year:	**£000**	£000	**£000**	£000
Trade debtors	**30,070**	37,100	**–**	–
Amounts owed by subsidiaries	**–**	–	**90,689**	90,552
Other debtors	**3,472**	20,686	**140**	14,865
Prepayments and accrued income	**3,153**	1,836	**125**	75
	36,695	59,622	**90,954**	105,492
Due after one year:				
Trade debtors	**–**	1,165	**–**	–
Other debtors	**31**	50	**–**	–
Prepayments and accrued income	**2,966**	4,519	**132**	121
	2,997	5,734	**132**	121
Total debtors	**39,692**	65,356	**91,086**	105,613

Included in trade debtors is £32.0m (2002: £38.1m) of invoiced long term contract costs less £23.9m (2002: £21.4m) of payments on account. Prepayments and accrued income due after one year include £2.4m (2002: £4.0m) in respect of the actuarial surpluses arising on the Group's UK defined benefit pension scheme.

18 Creditors due within one year

	Notes	Group 31 December 2003 £000	Group 31 December 2002 £000	Company 31 December 2003 £000	Company 31 December 2002 £000
Current instalments due on loans	20	**706**	791	**628**	519
Bank overdrafts		**–**	1,358	**40,111**	31,783
Advance receipts		**17,714**	43,478	**–**	–
Trade creditors		**61,408**	52,309	**126**	18
Finance lease obligations	20	**144**	99	**–**	–
Amounts owed to subsidiaries		**–**	–	**54,967**	32,364
Other creditors		**2,428**	10,245	**472**	313
Taxation		**2,534**	6,439	**869**	1,837
Payroll and other taxes including social security		**5,674**	2,961	**36**	117
Accruals and deferred income		**23,247**	15,826	**3,541**	3,406
Dividends		**–**	3,871	**–**	3,871
		113,855	137,377	**100,750**	74,228

19 Creditors due after one year

	Notes	Group 31 December 2003 £000	Group 31 December 2002 £000	Company 31 December 2003 £000	Company 31 December 2002 £000
Secured loans	20	**–**	4,673	**–**	4,673
Unsecured loans		**19,944**	16,018	**18,767**	15,000
Advance receipts		**20,621**	16,763	**–**	–
Other creditors		**258**	344	**60**	29
Finance lease obligations	20	**64**	62	**–**	–
		40,887	37,860	**18,827**	19,702

20 Secured creditors

Included within creditors are secured creditors as follows:	**Group 31 December 2003 £000**	Group 31 December 2002 £000	**Company 31 December 2003 £000**	Company 31 December 2002 £000
Creditors due within one year:				
Loan	**–**	519	**–**	519
Finance Leases	**144**	99	**–**	–
	144	618	**–**	519
Creditors due after one year:				
Loan	**–**	4,673	**–**	4,673
Finance Leases	**64**	62	**–**	–
	64	4,735	**–**	4,673
	208	5,353	**–**	5,192

The loan was secured over the assets of the Company and the Group. This security was released by Lloyds TSB during 2003 on renewal of the Group's banking facilities, being replaced by an omnibus guarantee and set-off agreement. This is further discussed in the Finance Director's Report. The finance leases are secured over the related leased assets.

21 Bank loans and overdrafts

Amounts falling due:	**Group 31 December 2003 £000**	Group 31 December 2002 £000	**Company 31 December 2003 £000**	Company 31 December 2002 £000
In one year or less or on demand:				
Bank overdrafts	**–**	1,358	**40,111**	31,783
Secured loan	**–**	519	**–**	519
Other unsecured loans	**706**	272	**628**	–
	706	2,149	**40,739**	32,302
Between one and two years:				
Secured loan	**–**	1,038	**–**	1,038
Other unsecured loans	**1,570**	271	**1,256**	–
Unsecured loan note	**15,000**	15,000	**15,000**	15,000
	16,570	16,309	**16,256**	16,038
Between two and five years:				
Secured loan	**–**	3,635	**–**	3,635
Other unsecured loans	**3,374**	747	**2,511**	–
	3,374	4,382	**2,511**	3,635
Total amounts falling due after one year	**19,944**	20,691	**18,767**	19,673
	20,650	22,840	**59,506**	51,975
Loans are analysed as follows:				
Bank overdrafts	**–**	1,358	**40,111**	31,783
Secured loan	**–**	5,192	**–**	5,192
Other unsecured loans	**5,650**	1,290	**4,395**	–
Unsecured loan note	**15,000**	15,000	**15,000**	15,000
	20,650	22,840	**59,506**	51,975

21 Bank loans and overdrafts (continued)

Other unsecured loans include:

(i) South African Rand (ZAR) 74,026,000 loan drawn down from Lloyds TSB in order to acquire the 75% interest in the equity share capital and shareholder loan of Alvis South Africa (Pty) Limited (formerly Vickers OMC) as part of the acquisition of Vickers Defence. The loan is repayable in bi-annual instalments over a five year period with the facility expiring in July 2007. Interest is incurred on the loan at 0.8% above the London Inter-bank Offering Rate (LIBOR) for ZAR, equating to 9.3% at 31 December 2003.
(ii) Minority shareholders' interest in the shareholder loan of Alvis South Africa (Pty) Limited. This loan is repayable over five years from 1 October 2002. The interest rate payable on this debt by Alvis South Africa (Pty) Limited is at the ZAR Prime Rate.

The unsecured loan note was issued to GKN plc on 2 November 1998 for an initial fixed period of three and a half years at a fixed rate of 7.75%. In February 2002, the Company exercised its option to extend the loan for a further three and a half years to 30 September 2005 at a fixed rate of 8.85%. The unsecured loan note has been disclosed as wholly repayable between one and two years in view of this extension.

The undrawn facilities in respect of which all conditions have been met for the Group and the Company at 31 December 2003 were as follows:

	Group	Group	Group	Company	Company	Company
	£ Sterling	Swedish Krona	South African Rand	£ Sterling	Swedish Krona	South African Rand
	£000	£000	£000	£000	£000	£000
Expiring in one year or less	60,000	88,756	3,358	60,000	–	268
Expiring in more than one year but not more than two years	–	–	268	–	–	268
Expiring in more than two years	–	–	803	–	–	803
	60,000	88,756	4,429	60,000	–	1,339

The purpose and terms of the facilities are discussed further in the Finance Director's Report.
The facilities are for both borrowing and bonding requirements.

22 Financial instruments

Disclosures on financial risk management, treasury policies and the use of financial instruments are included in the Finance Director's Report.

Short term debtors and creditors have been excluded from the following disclosures except for the analysis of net currency exposures.

a) Interest rate and currency profile of financial assets and liabilities

At 31 December 2003	**£ Sterling £000**	**Swedish Krona £000**	**US $ £000**	**South African Rand £000**	**Other £000**	**Total £000**
Financial assets:						
Cash and deposits, all at floating rates	**85,657**	**12,422**	**1,425**	**104**	**1,254**	**100,862**
Financial liabilities:						
Finance leases	–	**(208)**	–	–	–	**(208)**
Other unsecured loans	–	–	–	**(5,650)**	–	**(5,650)**
Unsecured loan stock	**(15,000)**	–	–	–	–	**(15,000)**
	(15,000)	**(208)**	–	**(5,650)**	–	**(20,858)**
At floating rate	–	**(208)**	–	**(5,650)**	–	**(5,858)**
At fixed rate	**(15,000)**	–	–	–	–	**(15,000)**
Weighted average fixed interest rate (%)	**8.85**					
Weighted average period for which rate is fixed (years)	**1.75**					
Net total	**70,657**	**12,214**	**1,425**	**(5,546)**	**1,254**	**80,004**
At floating rate	**85,657**	**12,214**	**1,425**	**(5,546)**	**1,254**	**95,004**
At fixed rate	**(15,000)**	–	–	–	–	**(15,000)**
	70,657	**12,214**	**1,425**	**(5,546)**	**1,254**	**80,004**

At 31 December 2002	£ Sterling £000	Swedish Krona £000	US $ £000	South African Rand £000	Other £000	Total £000
Financial assets:						
Cash and deposits, all at floating rates	25,805	30,884	1,816	–	29,831	88,336
Financial liabilities:						
Bank overdrafts	–	–	–	(1,358)	–	(1,358)
Secured loans and finance leases	–	(161)	–	(5,192)	–	(5,353)
Other unsecured loans	–	–	–	(1,290)	–	(1,290)
Unsecured loan stock	(15,000)	–	–	–	–	(15,000)
	(15,000)	(161)	–	(7,840)	–	(23,001)
At floating rate	–	(161)	–	(7,840)	–	(8,001)
At fixed rate	(15,000)	–	–	–	–	(15,000)
Weighted average fixed interest rate (%)	8.85					
Weighted average period for which rate is fixed (years)	2.75					
Net total	10,805	30,723	1,816	(7,840)	29,831	65,335
At floating rate	25,805	30,723	1,816	(7,840)	29,831	80,335
At fixed rate	(15,000)	–	–	–	–	(15,000)
	10,805	30,723	1,816	(7,840)	29,831	65,335

Interest payments on the floating rate assets and liabilities are determined at intervals of less than one year by reference to appropriate benchmark rates applicable in the relevant currency or market, such as LIBOR and STIBOR.

Alvis's policy in relation to interest rate risk is discussed in the Finance Director's Report.

22 Financial instruments (continued)

b) Currency exposure of net assets

Alvis's policy and objective in managing the currency exposure in its net investments overseas (structural currency exposure) is explained further in the Finance Director's Report. Gains and losses arising from these structural currency exposures are recognised in the statement of total recognised gains and losses.

The analysis below shows the Group's currency exposures in respect of transactional exposures (non-structural currency exposure) that give rise to the net currency gains and losses recognised in the profit and loss account. Such exposures comprise the net monetary assets and liabilities of the Group that were not denominated in the operating (or 'functional') currency of the operating unit involved.

The currency exposures at 31 December 2003 were as follows:

Functional currency of Group operation	**£ Sterling £000**	**Swedish Krona £000**	**US $ £000**	**South African Rand £000**	**Other £000**	**Total £000**
£ Sterling	**–**	**(165)**	**972**	**(629)**	**(1,310)**	**(1,132)**
Swedish Krona	**–**	**–**	**(289)**	**–**	**1,284**	**995**
South African Rand	**–**	**–**	**–**	**–**	**–**	**–**
Total	**–**	**(165)**	**683**	**(629)**	**(26)**	**(137)**

The currency exposures at 31 December 2002 were as follows:

Functional currency of Group operation	£ Sterling £000	Swedish Krona £000	US $ £000	South African Rand £000	Other £000	Total £000
£ Sterling	–	–	1,707	(1,322)	(786)	(401)
Swedish Krona	(278)	–	330	–	870	922
South African Rand	–	–	–	–	–	–
Total	(278)	–	2,037	(1,322)	84	521

The amounts shown in the table above, take into account the effect of forward foreign currency contracts entered into to manage these currency exposures.

c) Fair values

The estimated fair value of the Group's financial instruments are summarised below:

	At 31 December 2003		At 31 December 2002	
	Carrying amount £000	**Estimated fair value £000**	Carrying amount £000	Estimated fair value £000
Primary financial instruments held or issued to finance the Group's operations:				
Cash	**100,862**	**100,862**	88,336	88,336
Overdrafts	**–**	**–**	(1,358)	(1,358)
Loans due within one year	**(706)**	**(706)**	(791)	(791)
Loans due after one year	**(19,944)**	**(20,067)**	(20,691)	(20,854)
Finance leases (due within and after one year)	**(208)**	**(208)**	(161)	(161)
Derivative financial instruments held to hedge currency exposures on long term contracts:				
Forward foreign exchange contracts	**–**	**(6,021)**	–	(2,678)

Market values have been used to determine the fair value of forward foreign exchange contracts held to manage currency exposure. The fair values of all other items have been calculated by discounting the expected future cash flows at prevailing interest rates.

22 Financial instruments (continued)

d) Hedges of future transactions

The Group held contracts to exchange the following foreign currency amounts:

	Contract amount at 31 December 2003 £000	Contract amount at 31 December 2002 £000
Contracts to sell foreign currency against sterling	**72,551**	19,480
Contracts to purchase foreign currency against sterling	**23,734**	34,595
Contracts to sell/purchase foreign currency against other foreign currency	**4,337**	19,725

Unrecognised gains and losses on hedges on future transactions:

	Gains £000	**Losses £000**	**Net gains/ (losses) £000**
At 31 December 2001	5,402	(9,269)	(3,867)
Arising in previous year and recognised during 2002	(83)	161	78
Arising before 31 December 2001 and not recognised during 2002	5,319	(9,108)	(3,789)
Arising in 2002 and not recognised during the year	(3,709)	4,820	1,111
At 31 December 2002	1,610	(4,288)	(2,678)
Arising in previous year and recognised during 2003	(344)	(1,226)	(1,570)
Arising before 31 December 2002 and not recognised during 2003	1,266	(5,514)	(4,248)
Arising in 2003 and not recognised during the year	648	(2,421)	(1,773)
At 31 December 2003	**1,914**	**(7,935)**	**(6,021)**
Expected to be recognised:			
In one year or less	1,267	(4,061)	(2,794)
Between one and two years	383	(2,276)	(1,893)
Between two and three years	245	(901)	(656)
Between three and four years	19	(341)	(322)
Between four and five years	–	(340)	(340)
Later than five years	–	(16)	(16)
	1,914	(7,935)	(6,021)

The above contracts are all forward exchange rate contracts designed to hedge known purchases and sales on trading contracts which are in currencies other than the functional currency of the respective reporting business units.

23 Obligations under leases and hire purchase contracts

Amounts due under finance leases and hire purchase contracts:

	Group 31 December 2003 £000	Group 31 December 2002 £000	**Company 31 December 2003 £000**	Company 31 December 2002 £000
Amounts payable:				
Within one year	**144**	99	–	–
Between one and two years	**51**	50	–	–
Between two and five years	**13**	12	–	–
	208	161	–	–

23 Obligations under leases and hire purchase contracts (continued)

At the year end the annual commitments under non cancellable operating leases were as follows:

	Land and buildings 31 December 2003 £000	Land and buildings 31 December 2002 £000	**Other 31 December 2003 £000**	Other 31 December 2002 £000
Group				
Operating leases which expire:				
Within one year	**138**	266	**65**	330
Between one and five years	**170**	241	**330**	278
After five years	**1,142**	632	**–**	–
	1,450	1,139	**395**	608
Company				
Operating leases which expire:				
Within one year	**20**	3	**–**	3
Between one and five years	**–**	83	**6**	6
	20	86	**6**	9

24 Provisions for liabilities and charges

	Group Reorganisation provision £000	**Group Deferred taxation £000**	**Group Pension provisions £000**	**Group Other trading provisions £000**	**Group Total £000**	**Company Total £000**
At 31 December 2002	1,532	3,320	10,181	17,885	32,918	5
Charged in period	735	810	730	2,904	5,179	20
Released	–	–	–	(1,147)	(1,147)	–
Utilised	(1,565)	–	–	(2,918)	(4,483)	–
Acquisition of Vickers Defence	–	–	–	(223)	(223)	–
Exchange	–	202	917	427	1,546	–
At 31 December 2003	**702**	**4,332**	**11,828**	**16,928**	**33,790**	**25**

The Group reorganisation provision relates to the integration of the Alvis Vickers' businesses following the acquisition of Vickers Defence in September 2002. The provision remaining at 31 December 2003 is in respect of the latest stages of the restructuring and will be consumed within the coming financial year.

Group pension provisions relate to Alvis Hägglunds AB in Sweden. These provisions are very long term in nature and relate to the obligation of the business to the unfunded defined benefit pension fund in Sweden.

The other trading provisions included the following:

	31 December 2003 £000	31 December 2002 £000
Contract warranties	**8,194**	8,311
Other contract related provisions	**8,734**	9,574
	16,928	17,885

The contract warranty provisions are in respect of commitments for obligations made to customers under warranty for goods and services provided. The timing of these warranty commitments vary by product and customer, with none in excess of 6 years.
Other contract related provisions are obligations to customers outside of warranty which arise from past events. The timing of these commitments is variable and difficult to predict with any certainty.

24 Provisions for liabilities and charges (continued)

The analysis of deferred taxation is as follows:

	Amounts provided 31 December 2003 £000	**Amounts not provided 31 December 2003 £000**	Amounts provided 31 December 2002 £000	Amounts not provided 31 December 2002 £000
Accelerated capital allowances	**827**	**–**	429	–
Short term timing differences	**541**	**–**	291	–
Statutory taxation reserve	**2,224**	**–**	1,392	–
Pension surplus	**740**	**–**	1,208	–
Chargeable gain rolled over	**–**	**2,210**	–	2,210
	4,332	**2,210**	3,320	2,210

25 Share capital

	31 December 2003 £000	31 December 2002 £000
Authorised:		
171,817,424 Ordinary shares of 25p each	**42,954**	42,954
Allotted, called up and fully paid:		
110,278,945 Ordinary shares of 25p each	**27,570**	27,265

During the year, the issued ordinary share capital of the Company increased from £27,265,094 to £27,569,736 by the issue of 1,218,568 ordinary shares (2002: 498,323) of 25p each as a result of the exercise of options under Key Employee and SAYE share option schemes. The aggregate nominal value of the ordinary shares allotted was £304,642 (2002: £124,581) for consideration of £1,147,000 (2002: £595,000).

Share option schemes

At 31 December 2003, options under the Key Employee Share Option Scheme, Executive Share Option Scheme and the Save As You Earn (SAYE) share option scheme were outstanding in respect of a total of 4,789,534 ordinary shares as follows:

Date of grant	Number of shares	Exercise price per share
20 June 1997	8,875	132.4p
13 January 1998	130,000	161.5p
11 June 1998	600,000	194.0p
7 May 1999	96,674	138.5p
3 November 1999	1,101,500	127.5p
21 March 2000	575,000	100.0p
28 April 2000	394,626	72.4p
25 October 2000	280,000	81.5p
25 October 2000	280,000	117.5p
4 May 2001	10,000	128.5p
19 April 2002	331,767	108.8p
15 November 2002	260,400	137.5p
2 May 2003	543,692	126.0p
2 May 2003	177,000	163.5p

Options are exercisable between a minimum of three years and a specified maximum which is never longer than ten years from the date of grant.

26 Reserves

	Share premium account £000	Capital redemption reserve £000	Own shares reserve £000	Profit and loss account £000	Total £000
Group					
At 31 December 2002	1,164	37,014	–	(26,805)	11,373
Change of accounting for own shares held in trust	–	–	(5,533)	203	(5,330)
At 31 December 2002, as restated	1,164	37,014	(5,533)	(26,602)	6,043
Other recognised gains and losses (exchange)	–	–	–	302	302
Premium on issue of new shares	842	–	–	–	842
Movement in respect of recognition of costs of options over ordinary shares	–	–	–	(42)	(42)
Disposal of own shares held in trust	–	–	745	–	745
Profit retained in year	–	–	–	17,739	17,739
At 31 December 2003	**2,006**	**37,014**	**(4,788)**	**(8,603)**	**25,629**
Retained by:					
Company and subsidiaries	2,006	37,014	(4,788)	(8,681)	25,551
Joint ventures	–	–	–	78	78
	2,006	37,014	(4,788)	(8,603)	25,629

The own shares reserve is in respect of own shares held in trust by the Alvis Employee Benefit Trust.
The accumulated goodwill written off of £122.7m (31 December 2002: £122.7m) has been offset against the profit and loss account.

	Share premium account £000	Capital redemption reserve £000	Own shares reserve £000	Profit and loss account £000	Total £000
Company					
At 31 December 2002	1,164	37,014	–	70,163	108,341
Change of accounting for own shares held in trust	–	–	(5,533)	203	(5,330)
At 31 December 2002, as restated	1,164	37,014	(5,533)	70,366	103,011
Premium on issue of new shares	842	–	–	–	842
Movement in respect of recognition of costs of options over ordinary shares	–	–	–	(42)	(42)
Disposal of own shares held in trust	–	–	745	–	745
Profit retained in year	–	–	–	5,815	5,815
At 31 December 2003	**2,006**	**37,014**	**(4,788)**	**76,139**	**110,371**

Included in the profit and loss account of the Company are non-distributable reserves of £66.3m (2002: £67.4m).

The Group and Company have adopted during the period Urgent Issue Task Force (UITF) Abstract 38, Accounting for ESOP Trusts. As a result, the investment in Alvis plc ordinary shares through the Alvis Employee Benefit Trust (the trust) is no longer shown as an investment in own shares but is now shown as deduction from shareholders' funds. Consequently, any gain or loss on those shares by the Group and the Company is shown as a movement in shareholders' funds and not in either the profit and loss account or statement of total recognised gains and losses. Comparatives have been restated accordingly as follows.

Group

	Investments	Creditors due after one year	Net assets	Shareholders' funds
	£000	£000	£000	£000
31 December 2002 as previously reported	5,638	(38,063)	38,638	38,638
Adoption of UITF 38 at 1 January 2002	(5,406)	126	(5,280)	(5,280)
Movements during year ended 31 December 2002	(127)	77	(50)	(50)
Adoption of UITF 38 at 31 December 2002	(5,533)	203	(5,330)	(5,330)
31 December 2002 as restated	105	(37,860)	33,308	33,308

Company

	Investments	Debtors due after one year	Creditors due after one year	Net assets	Shareholders' funds
	£000	£000	£000	£000	£000
31 December 2002 as previously reported	110,395	105,314	(19,727)	135,606	135,606
Adoption of UITF 38 at 1 January 2002	(5,406)	101	75	(5,230)	(5,230)
Movements during year ended 31 December 2002	(127)	77	(50)	(100)	(100)
Adoption of UITF 38 at 31 December 2002	(5,533)	178	25	(5,330)	(5,330)
31 December 2002 as restated	104,862	105,492	(19,702)	130,276	130,276

Options granted to employees over shares held by the Alvis Employee Benefit Trust are charged to the profit and loss account in the year ended 31 December 2003 in accordance with UITF Abstract 17 (revised 2003), Employee Share Schemes. The effect of this change in accounting policy is not material on the profit and loss figures as presented in the year ended 31 December 2003 or the year ended 31 December 2002.

	31 December 2003	31 December 2002
	£000	£000
Market value of shares held in trust at year end	**6,265**	6,822
Number of shares held in trust	**3,642,440**	4,444,463
Number of share options outstanding over own shares held by trust	**2,740,961**	3,149,710

During the year, a net charge of £6,190 (2002: net charge of £8,437) in respect of operating the trust was recognised in the Company's profit and loss account. Dividends on the shares owned by the trust, the purchase of which was funded by a loan to the trust from Alvis plc, are waived.

27 Related party transactions

During the year the Group entered into the following trading transactions, in the ordinary course of business, with related parties:

	Sales to related party	Purchases from related party	Amounts owed to related party	Amounts owed by related party
Related party and Country of incorporation	£000	£000	£000	£000
ARTEC (Germany)				
2003	1,619	1,055	126	1,397
2002	10,965	1,165	357	3,804
Patria Hägglunds Oy (Finland)				
2003	12,246	146	–	5,150
2002	4,984	242	–	3,540
DGDT (South Africa)				
2003	–	–	41	–
2002	–	–	56	–

All transactions were at arms length.

At 31 December 2003, the Group owned 33.3% of ARTEC GmbH and 50.0% of Patria Hägglunds Oy. These interests are indirectly held by the Company. DGDT is the 25% minority shareholder in Alvis South Africa (Pty) Limited.

28 Pensions

The Group operates pension schemes in each of its businesses.

Current accounting for Group pension schemes

Business	Primary country of operation	Nature of pension scheme	Funding	Pension charge to the profit and loss account for the year ended 31 December 2003 £000	31 December 2002 £000	Net asset/(liability) recognised in the balance sheet as at 31 December 2003 £000	31 December 2002 £000
Alvis plc Alvis Vickers Alvis Bridging Alvis Ranges	United Kingdom	Defined benefit	Funded	**2,809**	1,114	**2,384**	4,027
Alvis Vickers	United Kingdom	Defined contribution	Funded	**–**	1	**–**	–
Alvis Hägglunds	Sweden	Multi-employer defined benefit	Funded	**736**	470	**–**	–
Alvis Hägglunds	Sweden	Multi-employer defined benefit	Unfunded	**730**	798	**(11,828)**	(10,181)
Alvis Hägglunds	Sweden	Multi-employer defined contribution	Funded	**870**	639	**(21)**	78
Alvis Moelv	Norway	Defined benefit	Funded	**203**	28	**–**	214
Alvis Moelv	Norway	Defined benefit	Unfunded	**19**	24	**(99)**	(98)
Alvis South Africa	South Africa	Multi-employer defined benefit	Funded	**56**	10	**–**	(6)
Alvis South Africa	South Africa	Multi-employer defined contribution	Funded	**329**	60	**(27)**	–
				5,752	3,144		

The increase in the Group pension cost reflects the inclusion of a full years charge in respect of the former Vickers Defence employees. It is not appropriate to show the total of the net assets/(liabilities) for all of the Group's pension schemes. The balances in respect of the Norwegian and South African pension schemes are included in accruals and prepayments as appropriate.

The schemes

United Kingdom - the Alvis Pension Scheme is a defined benefit scheme, operated on behalf of all the Group's UK businesses and open to all employees. The pension charge for the Alvis Pension Scheme is the annual regular cost of providing pension benefits to current employees, as adjusted for interest on the pension prepayment and variations arising from the latest actuarial assessment.

Sweden - employees participate in the pension scheme applicable to their employment category:
(a) Blue collar employees: pension benefits in excess of those provided by the state are governed by the SAF-LO Collective Pension, a defined contribution scheme.
(b) White collar employees: the supplementary pension for salaried employees in industry and commerce is known as ITP and is based on a collective agreement. It is primarily a defined benefit plan, although certain benefits are funded on defined contribution basis, including ITPK, a supplementary pension plan for higher paid employees. The defined benefit element of ITP is largely unfunded for current employees while all pensions in payment are funded by contributions from Alvis Hägglunds.
For both categories, the level of contribution is independently determined by the third party responsible for administering the pension benefits.

Norway - employees participate in one of two schemes, both defined benefit schemes, one employer funded, the other not funded by the employer.

South Africa - employees participate in the the pension scheme applicable to their employment category:
(a) White collar employees: pension provision is via a multi-employer defined contribution scheme.
(b) Blue collar employees: pension benefits are provided through membership of either the Engineering Industries Pension Fund (EIPF) or the Metal Industries Provident Fund (MIPF). The majority of blue collar employees are members of MIPF which is a multi-employer defined contribution scheme. The remainder are members of EIPF, a multi-employer defined benefit scheme. There is no difference between EIPF and MIPF in terms of the level of contribution made by the employer and employee. Because of the multi-employer nature of the EIPF scheme, it has been accounted for by the Group as a defined contribution scheme.

Explanation of net assets/(liabilities) recognised in the balance sheet

United Kingdom - the pension asset is disclosed as a prepayment due in greater than one year in accordance with SSAP 24 and as calculated by the actuaries of the Alvis Pension Scheme.

Sweden - the unfunded pension liability is disclosed within provisions and calculated by the Pension Registration Institute (PRI), an independent actuary and administrator of the ITP pension plan. In respect of the defined contribution scheme, the liability or asset in the balance sheet represents the employer contribution payable or prepaid respectively at the end of the year to the pension scheme.

Norway - the pension assets and liabilities shown are in accordance with actuarial estimates.

South Africa - the liability or asset in the balance sheet represents the employer contribution payable or prepaid respectively at the year end to the respective pension schemes.

Actuarial Valuations

An actuarial valuation of the Alvis Pension Scheme was carried out in April 2003. The principal assumptions adopted for the assessment were as follows. The comparatives for the last actuarial valuation in April 2000 are also disclosed.

	April 2003	April 2000
	%	%
Rate of return on investments	7.00	6.75
Rate of increase in salary	4.50	4.50
Rate of inflation	2.50	2.50
Market value of scheme assets (£m)	83.2	96.8
Assets as a percentage of scheme's accrued benefits	102%	108%

The impact of Financial Reporting Standard (FRS) 17 Retirement Benefits

The following disclosure relates to the Group's defined benefit schemes in the UK, Sweden and Norway.
The principal financial assumptions used by the independent qualified actuaries in updating the most recent valuations of the UK, Swedish and Norwegian defined benefit schemes for FRS 17 purposes were:

	31 December 2003			31 December 2002		
	UK	**Sweden**	**Norway**	UK	Sweden	Norway
	%	**%**	**%**	%	%	%
Rate of increase in salaries	**4.25**	**3.30**	**3.30**	4.00	3.05	3.30
Rate of increase in pensions	**2.75**	**2.20**	**2.50**	2.25	2.70	2.50
Discount rate	**5.50**	**4.00**	**7.00**	5.50	4.00	7.00
Inflation rate	**2.75**	**1.70**	**3.30**	2.25	3.00	3.30

28 Pensions (continued)

Since the Norwegian schemes are similar to one another in respect of assumptions, their disclosure is combined below.

The analysis of the assets in the UK scheme and the expected rates of return, plus the net assets and liabilities in the Norwegian scheme are as follows. The information for the disclosures below is not available in respect of Swedish unfunded benefit plan.

	31 December 2003			31 December 2002		
	UK Long-term investment return (%)	**UK Value £000**	**Norway Value £000**	UK Long-term investment return (%)	UK Value £000	Norway Value £000
Equities	**8.50**	**48,764**		8.50	38,450	
Bonds	**5.75**	**38,886**		6.50	36,045	
Property	**7.50**	**10,133**		7.50	8,919	
Total market value	**7.30**	**97,783**	**661**	7.50	83,414	716
Present value of scheme liabilities		**(106,520)**	**(598)**		(93,109)	(731)
Deficit in scheme		**(8,737)**	**63**		(9,695)	(15)
Related deferred tax		**2,621**	**(18)**		2,909	4
Net pension asset/(liability)		**(6,116)**	**45**		(6,786)	(11)

The movements during the year ended 31 December 2003 in respect of the FRS 17 net asset or net liability in the UK, Swedish and Norwegian pension schemes were as follows.

	UK £000	Sweden £000	Norway £000	Total £000
Net liability at 31 December 2002	(9,695)	(10,181)	(15)	(19,891)
Operating costs	(2,327)	(132)	(33)	(2,492)
Financing costs	1,090	(598)	12	504
Actuarial gain or loss	1,139	(341)	89	887
Employer contributions	1,056	341	11	1,408
Exchange	–	(917)	(1)	(918)
Net asset/(liability) at 31 December 2003	(8,737)	(11,828)	63	(20,502)

The net liability at 31 December 2003, net of deferred tax was £17,899,000 (2002: £16,978,000) and would be offset against the retained reserves, as disclosed below. There is no deferred tax in respect of the Swedish liability included in the net liability of the Group.

The South African defined benefit scheme (EIPF) is a multi-employer scheme for which the Group is unable to identify its share of the scheme's underlying assets and liabilities and consequently no disclosure in respect of FRS 17 can be made.

Under FRS 17 the actuarial gain disclosed above, would be shown as a movement in the Group statement of recognised gains and losses. Further information on this actuarial gain, which is not available in respect of the Swedish unfunded defined benefit plan, is given below.

At 31 December 2003	UK %	UK £000	Norway %	Norway £000
Difference between expected and actual return on assets	10.1	9,905	(8.5)	(56)
Change in assumptions	–	(5,783)	–	–
Experience gains and losses arising on scheme liabilities	(2.8)	(2,983)	24.2	145
Total actuarial gain or loss	1.1	1,139	14.9	89

28 Pensions (continued)

At 31 December 2002	UK %	UK £000	Norway %	Norway £000
Difference between expected and actual return on assets	(15.5)	(12,961)	(7.8)	(57)
Change in assumptions	–	(429)	–	–
Experience gains and losses arising on scheme liabilities	4.2	3,911	–	–
Total actuarial gain or loss	(10.4)	(9,479)	(7.7)	(57)

Percentages are expressed in terms of scheme assets/net present value of scheme liabilities as appropriate. If FRS 17 had been adopted in the Group's financial statements, the net assets and profit and loss account reserve, after taking account of deferred tax would be as follows:

	Adjustments in respect of accounting for FRS 17				**At 31 December 2003 Net assets/ reserves of Group**	At 31 December 2002 Net assets/ reserves of Group
	UK	Sweden	Norway	Total		
	£000	£000	£000	£000	**£000**	£000
Net assets					**53,199**	33,308
SSAP 24	(1,644)	11,828	99	10,283	**10,283**	6,154
					63,482	39,462
FRS 17	(6,116)	(11,828)	45	(17,899)	**(17,899)**	(16,982)
					45,583	22,480
Profit and loss reserve					**(8,603)**	(26,602)
SSAP 24	(1,644)	11,828	99	10,283	**10,283**	6,154
					1,680	(20,448)
FRS 17	(6,116)	(11,828)	45	(17,899)	**(17,899)**	(16,982)
					(16,219)	(37,430)

Additionally, if FRS 17 had been adopted in the Group's financial statements, these items would be disclosed as follows:

	Year ended 31 December 2003			Year ended 31 December 2002		
	UK	**Sweden**	**Norway**	UK	Sweden	Norway
	£000	**£000**	**£000**	£000	£000	£000
Within operating profit:						
Current service cost	**(2,327)**	**(132)**	**(23)**	(1,976)	(202)	(47)
Past service cost	–	–	–	–	–	(33)
	(2,327)	**(132)**	**(23)**	(1,976)	(202)	(80)
Within finance cost:						
Interest cost	**(5,087)**	**(598)**	**(40)**	(5,283)	(594)	(46)
Expected return on assets	**6,177**	–	**52**	6,375	–	52
	1,090	**(598)**	**12**	1,092	(594)	6
	(1,237)	**(730)**	**(11)**	(884)	(796)	(74)

Split of the Sweden costs is not available.

28 Pensions (continued)

The above FRS 17 disclosure in respect of the Alvis Pension Scheme in the UK does not reflect the likely transfer into the scheme of the past service entitlement of employees joining the Group following the acquisition of the Vickers Defence business on 30 September 2002. Almost all of these employees have joined the Alvis Pension Scheme in respect of their current service, the cost of which is reflected in the profit and loss account and pension disclosures. During the course of 2004, these employees will have the opportunity to transfer their past service entitlement and related assets from the Vickers Group Pension Scheme (VGPS) into the Alvis Pension Scheme. If 100 per cent of the former Vickers Defence employees were to transfer their past service entitlement, then the impact on an FRS 17 basis as at 31 December 2003 would have been as follows:

	Assets	Liabilities	Net liabilities
	£000	£000	£000
Alvis Pension Scheme	97,783	(106,520)	(8,737)
Bulk transfer from the VGPS	37,880	(44,343)	(6,463)
Alvis Pension Scheme (restated)	135,663	(150,863)	(15,200)

29 Contingent liabilities

Group

The following are contingent liabilities at the year end. They are not expected to give rise to any material financial loss.

	31 December 2003	31 December 2002
	£000	£000
Advance payment guarantees	**115,894**	120,627
Performance bonds	**13,138**	1,799
Others	**44,622**	23,422

All bonds and guarantees issued by the Group arise in the ordinary course of business. The bonds in the UK are secured from time to time by using specifically designated deposit accounts against the bonding drawn. Otherwise they are covered by an Omnibus Guarantee and Set-off Agreement (OGSA) covering the UK companies. The bonds in Sweden are secured through the overall security package of the Svenska Handelsbanken facility, including an Alvis plc guarantee, covenants and insurance. The bonds in South Africa are secured by an Alvis plc guarantee to Nedbank.

Proceedings have been brought against Group companies in respect of the Group's ordinary course of business. The Company and its legal advisors believe these proceedings will be successfully defended and are not expected to give rise to any material financial loss.

Company

The following are contingent liabilities at the year end.

	31 December 2003	31 December 2002
	£000	£000
Svenska Handelsbanken Guarantee	**23,291**	21,386
Nedbank Guarantee	**5,021**	4,343
Armscor Guarantee	**4,184**	3,620
Bonding in respect of trading contracts	**15,625**	7,308
	48,121	36,657

The guarantees issued by Alvis plc on behalf of subsidiary undertakings are in respect of the banking facilities in Sweden and South Africa and to Armscor (in South Africa) and are not expected to give rise to any material financial loss.

The trading guarantees are all secured by designated deposits given from time to time by the Company or by the OGSA of the UK Group and give rise to no contingent liability of the Company.

30 Notes to the Group Cash Flow Statement

a) Reconciliation of operating profit (excluding the Group's share of the results of joint ventures) to net cash inflow/(outflow) from operating activities

	Year ended 31 December 2003 £000	Year ended 31 December 2002 £000
Operating profit excluding the Group's share of the results of joint ventures	**18,237**	12,349
Depreciation of fixed assets	**7,337**	5,555
Amortisation of (negative goodwill)/goodwill	**(1,386)**	2
(Increase)/decrease in stocks	**(6,892)**	3,948
Decrease in debtors	**14,290**	4,984
Increase in creditors	**5,886**	6,760
Decrease in customer advances	**(30,095)**	(51,927)
(Decrease)/increase in provisions for liabilities and charges	**(458)**	2,253
Net cash inflow/(outflow) from operating activities	**6,919**	(16,076)

b) Analysis of changes in net funds

	At 31 December 2002 £000	Cash flow £000	Exchange £000	**At 31 December 2003 £000**
Current accounts, overnight deposits and cash	24,954	27,438	1,480	**53,872**
Overdrafts	(1,358)	1,570	(212)	–
	23,596	29,008	1,268	**53,872**
Time deposits	63,382	(19,635)	3,243	**46,990**
Cash at bank and in hand	86,978	9,373	4,511	**100,862**
Loans	(21,482)	1,820	(988)	**(20,650)**
Finance leases	(161)	(31)	(16)	**(208)**
	65,335	11,162	3,507	**80,004**

c) Acquisition of Vickers Defence

The Group acquired Vickers Defence on 30 September 2002. Vickers Defence comprised the businesses of Vickers Defence Systems, Vickers Bridging and a 75% interest in Vickers OMC. As stated in the 2002 Annual Report, the fair value adjustments at the time were estimated in some respects. The fair value adjustments have now been finalised during the year ended 31 December 2003 and are presented as follows.

	Balance sheet at date of acquisition £000	Fair value adjustments in the year ended 31 December 2002 £000	Fair value balance sheet as at 31 December 2002 £000	Fair value adjustments in the year ended 31 December 2003 £000	Reclassifications in the year ended 31 December 2003 £000	Final fair value balance sheet as at 31 December 2003 £000
Net assets acquired						
Intangible fixed assets	775	(775)	–	–	–	–
Tangible fixed assets	11,643	(65)	11,578	–	–	11,578
Other net current assets/(liabilities)	10,225	238	10,463	2,241	(16,091)	(3,387)
Net overdrafts	(1,252)	–	(1,252)	–	–	(1,252)
Deferred taxation	465	(871)	(406)	–	–	(406)
Other provisions for liabilities and charges	(2,061)	–	(2,061)	168	–	(1,893)
	19,795	(1,473)	18,322	2,409	(16,091)	4,640
Goodwill/(negative goodwill) (note 13)			257	(2,304)	–	(2,047)
Consideration			18,579	105	(16,091)	2,593
Satisfied by						
Cash			16,026	–	(15,964)	62
Deferred consideration			432	–	(127)	305
Costs of acquisition			2,121	105	–	2,226
			18,579	105	(16,091)	2,593

The net cash inflow in the year ended 31 December 2003 was £15.7m (2002: cash outflow £19.2m, including overdraft acquired of £1.2m), comprising a receipt from the vendor, Rolls-Royce, of £16.1m less costs and deferred consideration paid of £0.4m.

The fair value adjustment of £2.4m represents a reduction in creditors and provisions following assessment of contract balances acquired.

The reclassification of £16.1m represents the receipt from the vendor in respect of net current liabilities acquired which has been recognised as a reduction to purchase consideration.

The assets acquired and the consideration include amounts in respect of Alvis South Africa (Pty) Limited (formerly Vickers OMC). The exchange rate on acquisition was ZAR 16.58: £1.

Independent Auditors' Report to the Shareholders of Alvis plc

We have audited the Group's financial statements for the year ended 31 December 2003 which comprise the Group Profit and Loss Account, Group and Company Balance Sheets, Group Statement of Total Recognised Gains and Losses, Group Reconciliation of Movement in Shareholders' Funds, Group Cash Flow Statement, and the related Principal Accounting Policies and Notes 1 to 30. These financial statements have been prepared on the basis of the accounting policies set out therein. We have also audited the information in the Remuneration Report that is described as having been audited.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditors

The Directors are responsible for preparing the Annual Report, including the financial statements which are required to be prepared in accordance with applicable United Kingdom law and accounting standards as set out in the Directors' statement of responsibilities in relation to the financial statements.

Our responsibility is to audit the financial statements and the part of the Remuneration Report to be audited in accordance with relevant legal and regulatory requirements, United Kingdom Auditing Standards and the Listing Rules of the Financial Services Authority.

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Report of the Directors is not consistent with the financial statements, if the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law or the Listing Rules regarding Directors' remuneration and transactions with the Group is not disclosed.

We review whether the Corporate Governance Report reflects the Company's compliance with the seven provisions of the Combined Code specified for our review by the Listing Rules, and we report if it does not. We are not required to consider whether the Board's statements on internal control cover all risks and controls, or form an opinion on the effectiveness of the Group's corporate governance procedures or its risk and control procedures.

We read other information contained in the Annual Report and consider whether it is consistent with the audited financial statements. This other information comprises the Company Information, Chairman's Statement, Operations Review, Finance Director's Report, Report of the Directors, the unaudited part of the Remuneration Report and the Corporate Governance Report. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any other information.

Basis of audit opinion

We conducted our audit in accordance with United Kingdom Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements and the part of the Remuneration Report to be audited. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements and the part of the Remuneration Report to be audited are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements and the part of the Remuneration Report to be audited.

Opinion

In our opinion the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 2003 and of the profit of the Group for the year then ended and the financial statements and the part of the Remuneration Report to be audited have been properly prepared in accordance with the Companies Act 1985.

Ernst & Young LLP
Registered Auditor
London
10 March 2004

Principal activities

The principal activities of the Group are the design and manufacture of armoured and other specialist military vehicles. Further details appear on page 2.

Profit and dividends

The details of the results for the year, profit attributable to shareholders and the transfer to reserves are set out on page 22. The Directors are not recommending a final dividend for the year ended 31 December 2003 (2002: 3.7p). The interim dividend already paid gives a total dividend for the year of 2.5p per ordinary share (2002: 6.0p).

Share capital

There were no changes in the level of authorised share capital for the year. During the period, issued ordinary share capital of the Company increased from £27,265,094 to £27,569,736 by the issue of 1,218,568 ordinary shares of 25p each as a result of the exercise of options under Key Employee and SAYE share option schemes. The issued ordinary share capital at the end of the year was 110,278,945 shares of 25p each.

Business development

On 29 January 2004 the Company announced the closure of the Alvis Moelv business and the restructuring of Alvis Vickers' Telford site.

Research and development

The total expenditure in the year on non-customer funded research and development was £6.1m (2002: £5.4m) on projects described in the Operations Review.

Fixed assets

Changes in fixed assets during the year are summarised in notes 13, 14 and 15 on pages 36 to 38.

Substantial shareholdings

The Directors have been notified, pursuant to Sections 198-208 of the Companies Act 1985, of the following holders of 3% or more of the issued ordinary share capital of the Company as at 20 February 2004.

	Number of ordinary shares	Percentage of issued share capital
BAE Systems Plc	31,882,534	28.91
Schroder Investment Management Ltd	18,307,516	16.60
Fidelity Investments	9,509,438	8.62
Standard Life Investments	4,559,970	4.13
Hermes Pensions Management	3,773,894	3.42
Alvis Employee Benefit Trust	3,623,726	3.29

Shareholder analysis

Holdings of ordinary shares at 31 December 2003

Size of Holding	Number of Shareholders	% of Shareholders	Number of Shares	% of Shares
1,000,001 and above	19	0.74	83,343,620	75.58
500,001-1,000,000	9	0.35	6,639,108	6.02
100,001-500,000	52	2.03	11,457,488	10.39
50,001-100,000	27	1.06	1,900,744	1.72
1 - 50,000	2,453	95.82	6,937,985	6.29
Total	2,560	100.00	110,278,945	100.00

Directors

The biographical details of the Board and membership of Board committees is shown on page 3. The beneficial interests of the Directors in the share capital of the Company are shown in the Remuneration Report.

At the Annual General Meeting, Mr Beyer retires by rotation and Mr Wright retires by reason of his re-appointment to the Board since the last AGM. Both being eligible, they offer themselves for re-election.

Employment policies

The Group's employment policies include a commitment to equal opportunities regardless of sex, race, national or ethnic origin, religion or disability. With regard to employees who become disabled, reasonable steps, including retraining, are taken to ensure that they can remain in employment.

The Group attaches considerable importance to training, by both on-the-job and other training methods.

Alvis has a long history of employee involvement and it is the policy of the Group to maintain and develop that involvement. Consultation, participation and the provision of information concerning the Group takes place through formal and informal meetings, company newsletters and bulletins and discussions. Individual subsidiaries develop the practices best suited to their own circumstances.

Environmental policy

The Group has an Environmental Policy by which it is committed to compliance with environmental legislation, prevention of pollution and continual improvement of environmental performance at the Group's manufacturing sites worldwide. This is supported by site level policies and environmental action plans.

Donations

During 2003 the amount donated by the Group for charitable purposes in the UK was £13,507. £7,857 was donated to charities connected with the armed forces, £3,300 to charities related to children, medical and relief issues and £2,350 to other charitable organisations. No donations were made for political purposes.

Honours

Diane Thompson was awarded the MBE in the 2003 Queen's Birthday Honours List, and Patricia Birch was awarded the MBE in the 2004 New Year's Honours List.

Payment to suppliers

The Company and the operating businesses agree terms and conditions for their business transactions with suppliers. Payment is then made to these terms, subject to the terms and conditions being met by the supplier. Trade creditors of the Company at 31 December 2003 represented approximately 27 days purchases of the Company during the year ended 31 December 2003.

Registrars

Lloyds TSB act as Registrars for the Company. All communication regarding shareholdings should be sent to Lloyds TSB Registrars, The Causeway, Worthing, West Sussex BN99 6DA. Lloyds TSB Registrars also act as administrators to the Group's savings related share option scheme.

Auditors

A resolution to reappoint Ernst & Young LLP as auditors of the Company and to authorise the Directors to fix their remuneration will be proposed at the Annual General Meeting.

Notices of meetings

The Annual General Meeting will be held at noon, on Thursday 29 April 2004 in the Abraham Lincoln Room, at The Savoy, London. Notice of the Annual General Meeting together with an explanation of the special business to be considered at the meeting is contained in the Annual General Meeting circular enclosed with this annual report.

A copy of the minutes of last year's Annual General Meeting is available for inspection by shareholders at the registered address.

By order of the Board

P E Jarman
Secretary
10 March 2004

Information not subject to audit

The Remuneration Committee

The members of the Remuneration Committee during the financial year ended 31 December 2003 were Mr T J N Beyer, Mr D J Wright and Sir Robert Hayman-Joyce, all of whom are independent Non-executive Directors. Mr Wright joined the committee in December 2003 and the remaining members served on the committee throughout the year. The Committee's role is to set the terms of employment and emoluments of the Executive Directors, to approve all grants of discretionary share option awards and to advise the Board on and monitor remuneration for senior management. The Committee received relevant advice from Mr N M Prest (Chairman & Chief Executive) and Mr P E Jarman (Company Secretary).

Remuneration policy

The remuneration policy of the Board is to attract, retain and motivate Directors of the necessary calibre by rewarding them with competitive salary and benefits packages and to design these so as to align Directors' interests with those of the shareholders wherever possible. These packages are linked to individual and business performance and are reviewed each year to ensure they are supportive to the business objectives of the Group and the creation of shareholder value. Further details on the main elements of the policy are set out below. Directors' remuneration will be subject to regular review in accordance with this policy in the next and following years. Nevertheless, the Directors intend to continue to keep all elements of the policy under review and will, where appropriate, make changes to those elements in order to ensure that remuneration policy has the optimum structure.

Annual benefits

Annual benefits for Executive Directors comprise a basic salary, appropriate to the demands of the job, health and car benefits, and an annual discretionary incentive bonus. This is designed to focus on the importance of meeting the Company's targets and rewards achievement against established criteria, to encourage performance in a manner that the Remuneration Committee considers appropriate. The bonus is not pensionable. Non-executive Directors receive a fixed annual fee only and do not participate in any bonus scheme. Fees for Non-executive Directors are determined by the Board as a whole within the limits of the Articles of Association of the Company.

Longer term incentives

Executive Directors receive annual awards from the Company's Executive Share Option Scheme (ESOS) and may join the Company's SAYE Share Option Scheme.

ESOS options are exercisable after a minimum of at least three years and a specified maximum which will never be longer than ten years after they are granted. In awarding options, and in particular, in determining the number of shares over which an option under any discretionary share option scheme is granted, the Remuneration Committee will take into consideration the position of the employee within the organisation and his or her ability to influence the enhancement of shareholder value. This policy also applies to awards to Executive Directors under the scheme. Should the recommended offer referred to in the Chairman's Statement be unsuccessful and Alvis remain an independent company, ESOS options over shares with a market value of an amount not exceeding 150% of basic salary will be granted to the Executive Directors in 2004. Non-executive Directors are not permitted to participate in any of the Company's longer term incentive schemes.

In 1997, shareholders approved the rules of a Long Term Incentive Plan (LTIP). However, on reviewing the relative merits of this and other schemes, the Directors subsequently decided it was not in the Company's best interests to implement the LTIP. Although this decision is kept under review, the Directors do not currently consider that the LTIP forms part of the Company's remuneration policy.

Share Option Performance Conditions

The ESOS rules provide that options may only be exercised if there has been an increase in the Company's earnings per share ("EPS") over an initial three year period which is not less than the increase in the Retail Prices Index ("RPI") plus a percentage determined by the Remuneration Committee at the time of grant. For grants made in 2004, the required increase in excess of RPI will be 9% in respect of awards up to 100% of basic salary and 21% for awards in excess of this amount. If the performance condition is not satisfied at this point, re-testing is permitted on the first anniversary of the end of the initial three year period, but with an appropriately adjusted EPS target. For grants made in 2004, the re-test target will be 12% over RPI for awards up to 100% of basic salary and 28% over RPI for awards in excess of this amount. This performance condition was chosen in order to ensure that options would only become exercisable against the background of a sustained real increase in the financial performance of the Company. The Remuneration

Committee will determine whether the performance condition has been met using the EPS information contained in the Company's annual report and accounts, after taking the advice of the auditors as to whether any adjustments are required to ensure consistency in accordance with the terms of the performance condition. This method of determining whether a performance condition has been met was chosen because it is objective and readily demonstrable.

Balance between performance-related and other remuneration elements

The Board considers that the performance-related elements of the remuneration package, being bonus and share options, provide potentially the largest benefits to the Executive Directors.

Service Contracts

The Company's policy on the duration of Directors' contracts is that:

- Executive Directors should have rolling service contracts terminable on no more than one year's notice served by the Company or the Director;
- Non-executive Directors are appointed, where the Articles of Association of the Company permit, for fixed terms of usually 2 years, renewable on the agreement of both the Company and the Director.

Mr Prest's service contract and up to September 2003 Mr. Wright's letter of appointment have been exceptions to this policy. Mr Prest's contract does not conform to this policy as the policy was not implemented until 2001.

The Company does not normally make payments on termination of a Director's contract beyond its contractual obligations.

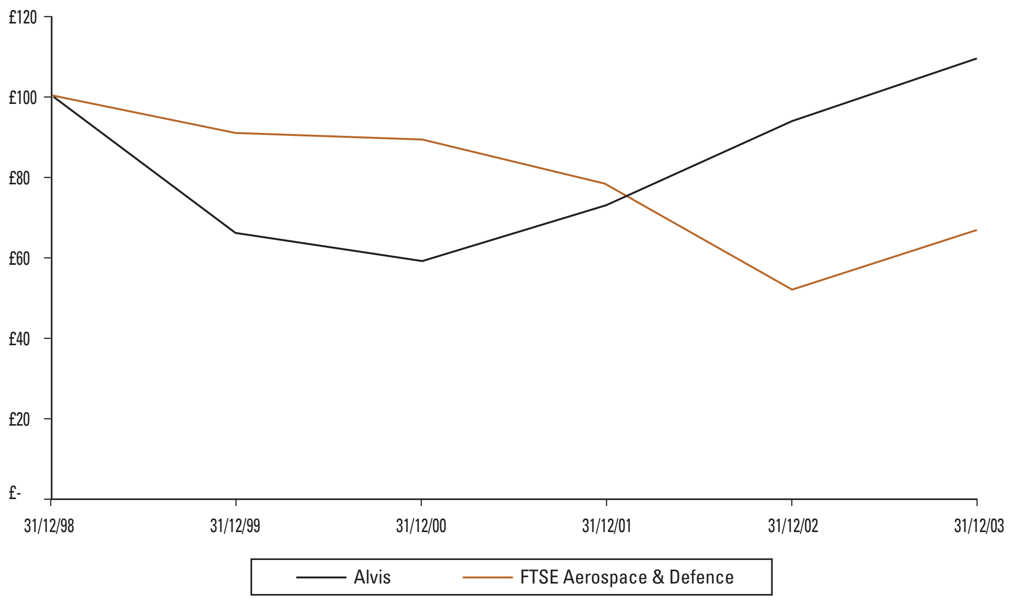
Post retirement benefits

Executive Directors are offered membership of the Alvis Pension Scheme, which is a defined benefit scheme. Non-executive Directors do not participate in the pension scheme.

Performance graph

The graph below shows a comparison of the total shareholder return for the Company's shares for each of the last 5 financial years against the total shareholder return for the companies comprised in the FTSE Defence and Aerospace Index. This Index was chosen for this comparison as it is a broad equity market index in which the Company is a constituent part and comprises other companies which operate in a similar industrial and commercial environment to Alvis.

Total Shareholder Return Alvis plc vs FTSE Aerospace and Defence



Directors' service contracts

Details of Directors' service contracts and letters of appointment are set out below. The terms and conditions of appointment of the Non-executive Directors are available for inspection during normal office hours on application to the Company Secretary.

Name	*Date of contract*	*Unexpired term (months)*	*Notice period (months)*	
N M Prest	4 May 1990	-	12/24	see Note 1
M F Greenslade	28 January 2000	-	12	
T J N Beyer	24 April 2003	13	-	
R Hayman-Joyce	15 July 2002	1	-	
D J Wright	6 January 2004	25	-	

Note 1: Mr Prest's contract specifies that the Company can terminate the contract after 31 December 2004 by giving 18 months' notice but any payment in lieu of notice will be equal to 90% of 18 months remuneration. Prior to that date, 24 months' notice must be given but any payment in lieu of notice will be equal to 18 months remuneration. Mr Prest can terminate the contract by giving 12 months' notice. Additionally, the contract specifies that in the event of a take-over, Mr Prest may terminate his contract by giving 3 months' notice at any time up to 9 months after the take-over. In these circumstances or if the Company terminates the contract within 2 years of the take-over (except where summary dismissal is applicable), Mr Prest is entitled to liquidated damages equal to 24 months salary and benefits (including bonus) if the take-over occurs after 31 March 2005 or 36 months before that date.

Information subject to audit

Directors' remuneration
Year to 31.12.2003

Executive Directors:	**Salary £**	**Fees £**	**Bonus £**	**Benefits £**	**Total 2003 £**	**Total 2002 £**
N M Prest	275,200	–	167,050	15,527	**457,777**	358,761
M F Greenslade	183,616	–	104,000	3,924	**291,540**	237,323
Non-executive Directors:						
T J N Beyer	–	27,500	–	–	**27,500**	22,500
R Hayman-Joyce	–	25,000	–	–	**25,000**	20,000
D J Wright	–	17,500	–	–	**17,500**	10,000
Total	458,816	70,000	271,050	19,451	**819,317**	648,584

Benefits include the provision of a fully expensed company car, private health insurance and miscellaneous expenses. Amounts stated as Bonus are reported on an accrued basis. N M Prest is the highest paid director for both years and received £457,777 before pension benefit (2002: £358,761).

Directors' pensions

The Executive Directors earned benefits in the Company's defined benefit pension scheme. The following table sets out the change in each Executive Director's accrued pension in the scheme during the year and his accrued benefits in the scheme at the year end.

	Changes in accrued pension during the year	**Transfer value of change**	**Accumulated total accrued pension at 31 December 2003**	**Accumulated total accrued pension at 31 December 2002**
	£p.a.	£	£p.a.	£p.a.
N M Prest	10,917	57,683	111,529	100,612
M F Greenslade	3,470	11,161	12,650	9,180

The following table sets out details of the cash equivalent transfer value of each Executive Director's accrued pension benefits in the scheme.

	At 31 December 2003	**At 31 December 2002**	**Change less directors' contributions**
	£	£	£
N M Prest	893,215	675,364	200,123
M F Greenslade	71,013	44,778	19,336

Notes

(a) Subject to Inland Revenue limits, the scheme provides for a maximum pension of two thirds of basic salary at normal retirement age together with dependents' pensions and a lump sum on death in service of four times basic salary. The pension in payment is protected by the application of Limited Price Indexation (LPI) for service after April 1999. Executive Directors contribute 7% of basic salary and the company makes up the balance of funding in respect of their pension provision. Directors may retire at any time after age 50 with the approval of the Company and the application of full actuarial reduction to their pension entitlement.

(b) The accumulated total accrued pension at 31 December 2002, after application of the LPI for the period to 31 December 2003, is £102,322 in respect of N M Prest and £9,336 in respect of M F Greenslade.

(c) The pension entitlement shown is that which would be paid annually on retirement, based on service to the end of the year.

(d) The increase in accrued pension during the year, excluding any increase for inflation, is £9,207 in respect of N M Prest and £3,314 in respect of M F Greenslade.

(e) The transfer value has been calculated on the basis of actuarial advice in accordance with Actuarial Guidance Note GN11 less Director's contributions.

(f) Members of the scheme have the option to pay Additional Voluntary Contributions; neither the contributions nor the resulting benefits are included in the above table.

(g) No element of remuneration other than basic salary is pensionable.

Directors' interests

Ordinary shares

The beneficial interests of the Directors, including family interests, in the ordinary shares of the Company as at 31 December 2003 were as follows:

	31.12.03	**31.12.02**
N M Prest	**1,031,434**	1,000,655
M F Greenslade	**232,279**	100,000
T J N Beyer	**80,000**	80,000
D J Wright	**62,698**	49,584
R Hayman-Joyce	**21,927**	16,927

The Executive Directors, as potential beneficiaries, are deemed to have an interest in the ordinary shares of the Company held from time to time by the Alvis Employee Benefit Trust established to facilitate the operation of the Company's various share option schemes. At 31 December 2003 the trust held 3,642,440 ordinary shares (2002: 4,444,463 ordinary shares).

Share options

In the following tables, "KESOS" means the Company's Key Employee Share Option Scheme, "Super" means a Super Option under the KESOS rules, "ESOS" means the Company's Executive Share Option Scheme and "SAYE" means the Company's Inland Revenue approved Savings Related Share Option Scheme.

N M Prest

Type of option	**Exercise price per share**	**Exercisable**	**Performance Condition**	**No. at 1 January 2003**	**Awarded during the year**	**Exercised during the year**	**Market price at date of exercise**	**Expired unexercised during the year**	**No. at 31 December 2003**
ESOS	163.5p	02.05.06 - 01.05.13	See Note 2	–	118,000	–	–	–	118,000
Super	194p see Note 1	11.06.03 - 11.06.08	See Note 3	600,000	–	–	–	–	600,000
KESOS	127.5p	03.11.02 - 02.11.09	None	200,000	–	(23,500)	191p	–	176,500
KESOS	81.5p	25.10.03 - 24.10.04	None	185,000	–	–	–	–	185,000
KESOS	117.5p	01.04.04 - 31.03.05	None	185,000	–	–	–	–	185,000
KESOS	137.5p	15.11.05 - 14.11.06	None	130,000	–	–	–	–	130,000
SAYE	72.4p	01.07.03 - 31.12.03	None	7,279	–	(7,279)	201p	–	–
SAYE	118p	01.07.06 - 31.12.06	None	6,521	–	–	–	–	6,521
SAYE	126p	01.07.08.-.31.12.08	None	–	2,815	–	–	–	2,815

M F Greenslade									
Type of option	**Exercise price per share**	**Exercisable**	**Performance Condition**	**No. at 1 January 2003**	**Awarded during the year**	**Exercised during the year**	**Market price at date of exercise**	**Expired unexercised during the year**	**No. at 31 December 2003**
ESOS	163.5p	02.05.06 - 01.05.13	See Note 2	–	59,000	–	–	–	59,000
Super	100p	21.03.05 - 21.03.10	See Note 3	300,000	–	–	–	–	300,000
KESOS	100p	21.03.03 - 20.03.10	None	300,000	–	(125,000)	158.5p	–	175,000
KESOS	100p	21.03.04 - 20.03.10	None	100,000	–	–	–	–	100,000
KESOS	81.5p	25.10.03 - 24.10.04	None	95,000	–	–	–	–	95,000
KESOS	117.5p	01.04.04 - 31.03.05	None	95,000	–	–	–	–	95,000
KESOS	137.5p	15.11.05 - 14.11.06	None	65,000	–	–	–	–	65,000
SAYE	72.4p	01.07.03 - 31.12.03	None	7,279	–	(7,279)	185p	–	–
SAYE	118p	01.07.04 - 31.12.04	None	3,743	–	–	–	–	3,743
SAYE	126p	01.07.06 - 31.12.06	None	–	1,620	–	–	–	1,620

Note 1: Under arrangements entered into with the Company in 1998, Mr Prest will effectively be put in the same financial position as if the option exercise price were 133.5p.

Note 2: The performance condition is that the Company's earnings per share must increase between either 2002 and 2005 by the same percentage as the retail prices index plus 9% or, failing that, between 2002 and 2006 by the same percentage as the retail prices index plus 12%.

Note 3: The performance condition is that over a 5 year period the Company's earnings per share growth is in the upper quartile when measured against the FTSE 100.

The market price of the Alvis ordinary share at 31 December 2003 was 172p, the highest market price during the financial year was 220p and the lowest was 144p.

Changes in Directors' interests

There have been no changes in the Directors' interests in shares or options between 31 December 2003 and 10 March 2004.

Approval of Remuneration Report

This Remuneration Report was approved by the Board on 10 March 2004.

T J N Beyer

Chairman, Remuneration Committee

On behalf of the Board of Alvis plc

Corporate Governance Report

The Combined Code on Corporate Governance, and related guidance, sets out principles of best practice. The paragraphs below, together with the Remuneration Report, describe how the Code is applied within Alvis.

The Board

The Alvis Board currently comprises two Executive and three Non-executive Directors and reflects a blend of different ages, experience, backgrounds and cultures. In the opinion of the Board, all three Non-executive Directors are independent of management and free from any business or other relationship which could materially interfere with the exercise of their independent judgement. Mr Beyer has shown, by his contribution to the Board, that he has always exercised independent judgement. The Board considers that Mr Beyer's ten years' service on the Board has not affected this. Mr Wright was originally appointed a Director as the nominee of GKN. Since the sale of GKN's shareholding in September 2003, Mr Wright has remained on the Board without any connection to any significant shareholder and since that time the Board considers him to be independent.

The Board reserves to itself approval of matters that are of major concern to the Group including Group strategy, annual budgets, acquisition and disposal of material assets, commitment to various types of expenditure and the acceptance of contracts above established authority levels. Remaining decisions are delegated to senior management.

Mr Prest acts as the Chairman and Chief Executive of the Company. He has no other significant commitments. The Board believes that combining the roles of Chairman and Chief Executive is appropriate for a Company of Alvis's size and market position at the present time as it enables the Company to react swiftly and decisively to developments in a rapidly changing industry. This arrangement is considered to be appropriate because of the balance provided by a strong and independent Non-executive element on the Board. In particular, Non-executive Directors form the majority of the Board. Key decisions are expressly reserved to the full Board and power is delegated to the Executive Directors only in defined circumstances. The roles of the active Remuneration and Audit Committees have been clearly defined, and these Committees (comprising only Non-executive Directors) play an important and prominent part in the governance of the Company. Mr Beyer is the Board's recognised senior independent Non-executive Director to whom concerns can be conveyed should they arise. Taken as a whole, the Board considers that these arrangements provide Alvis with the optimum combination of effective leadership and checks and balances.

The Board normally meets at least four times a year and where possible at least one meeting is held at the site of one of the Group's operating subsidiaries. Comprehensive briefing papers on items for consideration are circulated to each Director. As is usually the case, there have been no absences from either full Board meetings or the meetings of any Board Committee during 2003.

Each of the Directors is required ordinarily to retire by rotation at least once every three years.

The performance of the Board, its Committees and each of the Directors is continuously evaluated by all Board members through open discussion and exchange of views during the course of the year. Mr Beyer, as senior independent director, is responsible for evaluating Mr Prest's performance as Chairman.

The Executive Directors regularly met with representatives of major shareholders in order to ensure that the Board has a good understanding of their views.

Specific responsibilities have been delegated to a number of Board Committees.

Audit Committee

The Committee comprises all the Non-executive Directors under the Chairmanship of Mr Wright. All members are considered by the Board to be independent. The terms of reference of the Audit Committee are available on the Company's website. The Committee met three times in 2003 and, with the external auditors, examined the process of financial reporting, the scope and the results of the audit and any changes to accounting policies. It also reviewed the terms of reference and results of the Internal Control Committee.

During 2003, the external auditors provided a number of non-audit services. The Audit Committee is responsible for ensuring that auditor objectivity and independence is maintained. It does so by ensuring that the non-audit work which the auditors are asked to carry out is limited as much as possible. In particular, any such work is restricted to occasions where it is believed that the Company will accrue a very substantial benefit (either in terms of cost or effectiveness) because of the auditors' knowledge and understanding of the Company's affairs.

Remuneration Committee

The Committee comprises all the Non-executive Directors under the Chairmanship of Mr Beyer. All members are considered by the Board to be independent. During 2003 it met three times. The terms of reference of the Committee are available on the Company's website. It is responsible for setting the remuneration of the Executive Directors and advising and recommending to the Board general policy on remuneration for senior management. Further details appear in the Remuneration Report.

Nominations Committee

The Committee currently comprises the entire Board under the Chairmanship of Mr Beyer. The majority of the Committee are independent Non-executive Directors. The terms of reference of the Committee are available on the Company's website. It is responsible for leading the process for Board appointments. The Committee met once during 2003 and concluded that no new appointments to the Board were currently necessary.

Group Executive Committee

The Committee comprises the Executive Directors and senior managers from across the Group and meets four times a year. It provides a forum for the discussion and review of business unit and Group issues.

Shareholder communications

Meetings between Directors, senior management and major institutional shareholders are held periodically and when required in relation to particular issues. Shareholders attending the AGM are invited to ask questions concerning the Company's business and to meet Directors after the formal proceedings have ended.

In its annual and interim reports, results presentations and city announcements generally, Alvis endeavours to present an accurate, objective and balanced picture in a style and format which is appropriate for the intended audience.

The Company's website provides financial and business information about the Group.

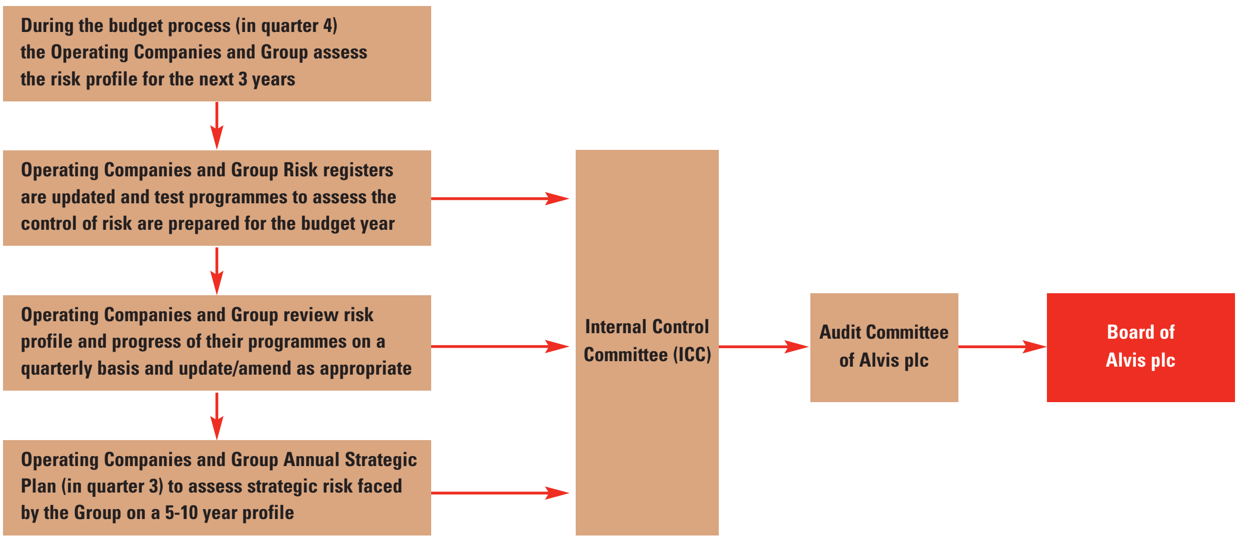
Internal control

The Board acknowledges that it is responsible for the Group's system of internal control and for reviewing its effectiveness. Such a review was carried out in 2003. A system of internal control can only provide reasonable assurance and not absolute assurance against material misstatement or loss, as it is designed to manage rather than eliminate the risk of failure to achieve business objectives.

The Board has always attached considerable importance to the Group's system of internal control and risk management. This is managed through a number of policies and procedures at local operating company level and Group level:

- a comprehensive formal review structure at local operating company level and at Group level which considers a variety of risk issues in depth as part of the management of the business (these include project reviews and operations reviews)
- well defined procedures governing the appraisal and approval of investments
- a comprehensive system of financial reporting to the Board (which includes an annual budget cycle, quarterly re-forecasting and monthly reporting)
- annual strategic planning cycle
- appointment of experienced and professional staff, both by recruitment and promotion, of the necessary calibre to fulfil their allotted responsibilities
- comprehensive manuals of policies and procedures

Risk Review Process



Internal reporting procedures are based on a system of positive confirmation rather than exception reporting. In addition to the policies and procedures referred to above, risk reporting is based on the compilation and monitoring of comprehensive risk registers. This is embedded in the business through an annual and quarterly review process.

The Board has delegated responsibility for implementing the system of internal control to the Boards of the local operating companies and to the Group Executive Committee in respect of Group issues. However, it is co-ordinated and monitored across the Group by the Internal Control Committee (ICC); the scope, role and output of the ICC is reviewed by the Audit Committee twice each year. The Board has considered creating a Group internal audit function, but at this stage of the Group's development considers that this is not appropriate.

The Group participates in a number of joint ventures. As the Group cannot exercise complete control over these operations, the review of internal control has been less comprehensive in such cases. However, wherever possible, the Group has sought to influence management practices.

The Board has reviewed the effectiveness of the system of internal control in operation in the Group for the period covered by the accounts and it considers that a system compliant with the Combined Code and associated Guidance has been in place throughout the year 2003 and continues up to the date of approval of the Report and Accounts.

Going concern

After making enquiries, the Directors have a reasonable expectation that the Group and the Company have adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Directors' statement of responsibilities

Company law requires the Directors to prepare accounts for each financial year which give a true and fair view of the state of affairs of the Company and of the Group and of the profit and loss of the Group for that period. In preparing those accounts, the Directors are required to select suitable accounting policies and then apply them consistently; make judgements and estimates that are reasonable and prudent; and state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts. The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and to enable them to ensure that the accounts comply with the Companies Act 1985. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Compliance

The Board considers that, with the exceptions set out below, the Company has complied with the relevant provisions of the Combined Code throughout the financial year 2003:

Notice periods Although it is now the Board's policy that all new service agreements for Executive Directors should have notice periods of one year or less, the Board has not adopted this objective in relation to Mr Prest's contract as it pre-dates the adoption of this policy. Further details appear in the Remuneration Report.

Fixed term non-executive contracts During the 2003 financial year, all the Non-executive Directors have fixed term service contracts set out in letters of appointment, except Mr Wright. Until September 2003 Mr Wright's appointment as a Director was not for a specified term but was terminable, in accordance with the Company's Articles of Association, by GKN giving notice to the Company. Following GKN's disposal of its shareholding in the Company, Mr Wright's appointment ceased to be terminable by GKN and is now subject to a letter of appointment expiring at the AGM in 2006.

Alvis plc corporate details and advisers

Alvis plc
Registered Office
34 Grosvenor Gardens
London
SW1W 0AL

Tel: +44 (0)20 7808 8888

Fax: +44 (0)20 7808 8877

E-mail: info@alvis.plc.uk

Web: www.alvis.plc.uk

Registered Number 731159

Alvis Vickers Limited
Scotswood Road
Newcastle-upon-Tyne
NE99 1BX

Alvis Bridging Limited
Spring Road
Ettingshall
Wolverhampton
WV4 6YN

Alvis South Africa (Pty) Limited
12 Barnsley Road
Benoni 1500
South Africa

Alvis Hägglunds AB
SE-891 82
Örnsköldsvik
Sweden

Auditors
Ernst & Young LLP

Bankers
Lloyds TSB Bank Plc
Svenska Handelsbanken AB (publ)

Merchant Bankers
Lazard & Co, Ltd

Stockbrokers
Hoare Govett

Legal Advisers
Eversheds

Registrars
Lloyds TSB Registrars
The Causeway
Worthing
West Sussex
BN99 6DA